Quarterly report on the Spanish economy

1. Overview

Into the year 2000, the Spanish economy has been sustaining a high growth rate. The well-rooted expansion of foreign markets and the continuing buoyancy of domestic demand have, on Banco de España estimates, placed the year-on-year growth rate of real GDP at 4 % in the first quarter, slightly up on the initial rate released by INE (National Statistics Institute) for the final quarter of 1999. The climate of growth is likewise the case for the other euro-area economies, according to the indicators available for the opening months of the year. The 12-month growth rate of the harmonised index of consumer prices (HICP) for the area has continued accelerating. It stood at 2.1 % in March (3 % in the Spanish economy), due essentially in both cases to the rise in energy prices, the effect of which reached its height in the preceding months.

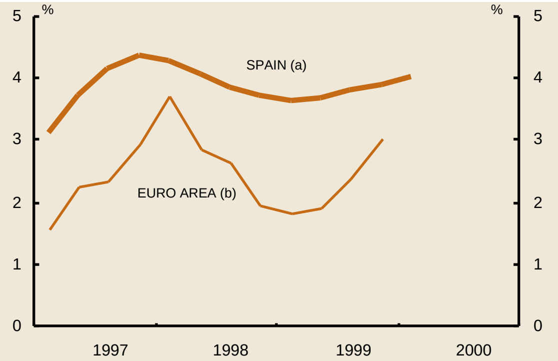
Charts 1 and 3 show that the gap between the growth rate of the Spanish economy and that of the euro area as a whole is narrowing, while the differences between the growth rates of consumer prices, measured via harmonised indices, have been cut slightly. Underpinning the notable pick-up in the euro-area economies is, on one hand, the expansionary impact of the external environment and, on the other, the increasingly firm recovery (albeit still of differing intensity from country to country) in domestic demand. Yet in the Spanish economy, despite the improvement in the contribution of net external demand being on a similar scale, what was already a high growth rate of domestic demand is moderating, after four years of notable vigour.

For 2000 Q1, it is estimated that real national demand in the Spanish economy may have posted a rate of around 4.5 % year-on-year, with a negative contribution of net external demand of approximately half a percentage point. Assessment of these data, on comparing them with 1999 Q4, requires caution as the INE figures could be altered once information not available at the time of their release is incorporated. The trend discernible in the indicators underpinning these estimates points to a stabilising or moderate loss of momentum of the year-on-year growth rate of domestic demand in the final months of the current year, and to an improvement in the negative contribution of the net external balance.

The continuation of the growth phase in the US economy has played a pivotal role in extending the expansionary climate to virtually all the main economic areas, with the notable exception of Japan. The macroeconomic and financial stability attained (or progress towards it) in many of these countries has been a fundamental factor in this favourable environment be-

CHART 1

Gross domestic product



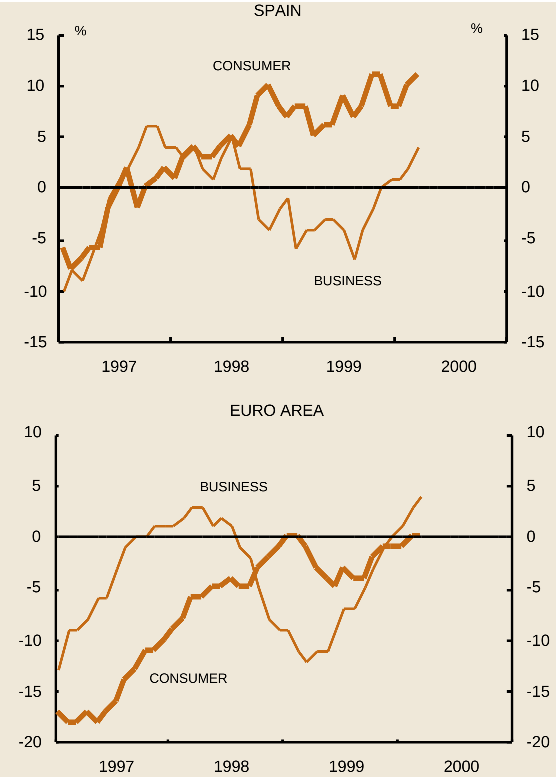
Sources: ECB, Instituto Nacional de Estadística and Banco de España.

(a) Non-centred annual rate of change calculated on the basis of the trend-cycle series.

(b) Non-centred annual rate of change calculated on the basis of the seasonally adjusted series.

CHART 2

Confidence indicators



Source: European Commission.

coming a generalised feature. And a further underlying factor has been the spread of significant technological advances taking place in key sectors of these economies. The surge in the prices of energy products since mid-1999 has posed a threat to the stability marking this process. Although the latest developments on the market for crude oil are tending to ease the pressures generated, the impact of the increases recorded has yet to run its full course and, in addition, regard must be had to the ongoing rise in the prices of other commodities and of certain manufactures. These effects are felt most sharply in the economies whose currencies have depreciated or which are ahead in the growth cycle.

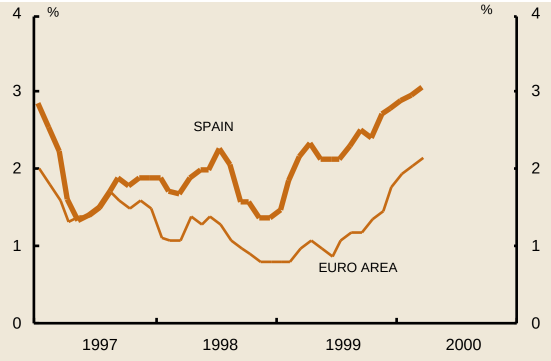
As stated, the 12-month growth rate of the HICP for the euro-area countries was 2.1 % in March, approximately one percentage point up on the related rate in mid-1999. The strong increase in energy product prices on international markets, exacerbated by higher import prices further to the depreciation of the euro, was to a large extent the determining factor here. The change in the future price outlook, the firming of the recovery in economic activity across the area and the persisting high growth rates of monetary and credit aggregates (the assessment of which requires looking beyond the influence of the temporary factors in place during the monetary union's first year of life) all bore on euro-area monetary policy. The European Central Bank (ECB) decided to continue in February and March with the gradual pattern of rises first initiated in November last year, taking its benchmark interest rate to 3.5 %. These interest rate movements had already been discounted by the money markets which, in turn, brought forward their expectations about future upward movements. Financial markets and, in particular, stock markets were also influenced by the volatility stemming from the US markets.

The fiscal policy stance of most of the euro-area economies enabled the overall general government deficit to be cut to 1.2 % of GDP in 1999. The fresh cuts envisaged for the current year should have a bearing, above all, on the effective control of spending. Wage negotiations for the year have not confirmed the fears that the high demands in Germany had aroused. And this, combined with favourable expectations about crude oil prices and with the response of the monetary authorities, is shaping an environment more conducive to an easing of pressure on consumer prices in the second half of the year.

The generous monetary and financial conditions that continue to prevail across the euro area are feeding through to the Spanish economy and affecting it due to its particular position ahead in the cycle. The narrow aggregates, those most directly related to spending deci-

CHART 3

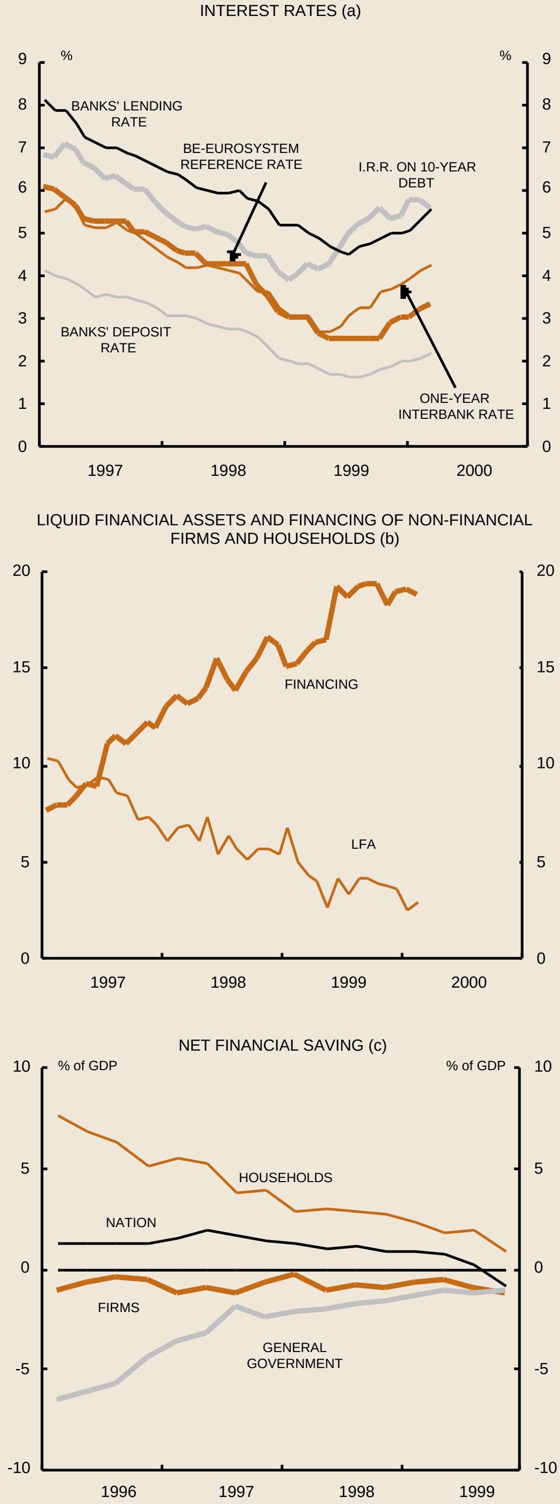
Harmonised índices of consumer prices



Sources: Eurostat and European Central Bank.

CHART 4

Financial indicators of the Spanish economy



Source: Banco de España.
(a) The series are averages of daily data.
(b) Financing includes bank loans extended by resident and non-resident credit institutions and fixed-income securities.
(c) Cumulative data over past four quarters.

sions, posted the highest rates of increase in the early months of the year, and the growth of financing to the private sector remained very high at around 19 %, far outstripping the rate for the area as a whole (see Chart 4). As regards fiscal policy, the end-1999 result was an overall general government deficit of 1.1 % of GDP, which was better than expected. The figures on the State budget outturn in 2000 Q1 also show a favourable trend. Notable on the revenue side is the continuing positive performance of indirect tax, which is closely linked to the buoyancy of economic activity. The strong increase in expenditure is due, in turn, to the concentration in these months of heavy interest payments. Indeed, if the period allocation of this expenditure is made in accordance with National Accounts criteria, the results are very positive, namely a slight deficit during Q1 similar to that of the same period a year earlier.

Against this background, in which greater export buoyancy has added to the factors driving domestic spending, final demand in the economy is estimated to have run at an annual rate of around 6 % in real terms during 2000 Q1, exceeding the related figure for 1999. The acceleration in output was, as earlier stated, less intense since approximately two percentage points of the growth of demand leaked out to the foreign sector, via the increase in imports.

Notable among the national demand components was the vigour of private consumption, as most of the indicators released show. The factors behind high growth rates in real consumption for the third year running remain essentially unchanged. They include the rise in real disposable income, low real interest rates, gains in wealth and favourable consumer expectations.

Of particular significance in these opening months of the year is the expansionary impact of wage- and pension-related inflation-adjustment mechanisms (which pass through to current-year revenue the differences between the previous year's forecast and actual consumer price growth) on household income. Such differences largely arose from the increase in the prices of energy products. Attempts to avoid the losses in real income deriving from external shocks prove unfruitful in the medium run and may have undesirable consequences for the inflation rate. The increase in consumer spending and the notable buoyancy of investment in housing (where only the initial signs of a slowdown can be seen) are reducing households' lending capacity. This is confirmed by the estimate of their net financial saving which, at the end of last year, was at historically low levels.

The slowdown in construction investment, which is less than expected some months back owing, perhaps, to the firmness of investment in housing, is therefore due to the course of public works, the growth rate of which began to fall in mid-1999. Capital investment, for its part, is running on similar lines to 1999 Q4, having gradually slowed over the course of last year. Robust final demand in the economy and the favourable corporate conditions prevailing are reflected in the positive expectations about the future course of investment shown by most surveys.

The pick-up in goods exports is, as commented, proving to be a key factor in the intensifying growth rate of the Spanish economy in the opening months of the year, as it is in the other euro-area economies. Adding to the impetus given by non-euro area markets and by the weakness of the euro is the boost provided by the growing buoyancy of intra-Community trade, as some of the more lagging economies in the area join the process. The persistence of high real growth rates for imports, accentuated by the surge in import prices, is further widening the current-account deficit, despite the fact that other associated components (particularly tourism and transfers) are contributing to its containment.

Employment developments in the early months of 2000 are corroborating the strength of economic activity, which is common to virtually all branches of industry. The moderate slowdown dating back to last year in the rate at which new net jobs are being created does not appear to have intensified, and is providing for a gradual recovery in apparent labour productivity. This, in turn, is preventing the rise in wages – the consequence, to date, of the effect of wage-adjustment mechanisms and of collective bargaining agreements spanning several years (the information on new agreements is as yet scant) – from passing through in full to unit labour costs. The growth rate of this latter variable, which is higher than that of most euro-area countries, is not substantially different from that posted last year.

Turning to price developments, the 12-month growth rate of the consumer price index (CPI) has stabilised at close to 3 % in Q1, owing essentially to the effect of higher energy prices. Food prices are generally trending favourably, while the rate of increase of non-energy industrial goods has turned considerably up, widening the gap (as measured by the HICP) with the euro-area countries. The service inflation differential, however, is narrowing slightly, as the related growth rate has accelerated across the area while holding stable in the Spanish economy.

The circumstances surrounding the Spanish economy's performance so far in the year 2000 are not substantially different from those prevailing at the end of 1999. First, the pick-up in the external environment is firming and growth expectations for the world economy are being revised upwards. Next, price pressures persist on certain commodities markets which, in the case of energy products, are tending to ease. Further, monetary and financial conditions are particularly generous, although there has been a change of tack in the euro area-wide monetary policy stance. And finally, the shortfall in public finances continues to abate, favoured by the increases in revenue that the buoyancy of economic activity entails.

2. The external environment of the euro area

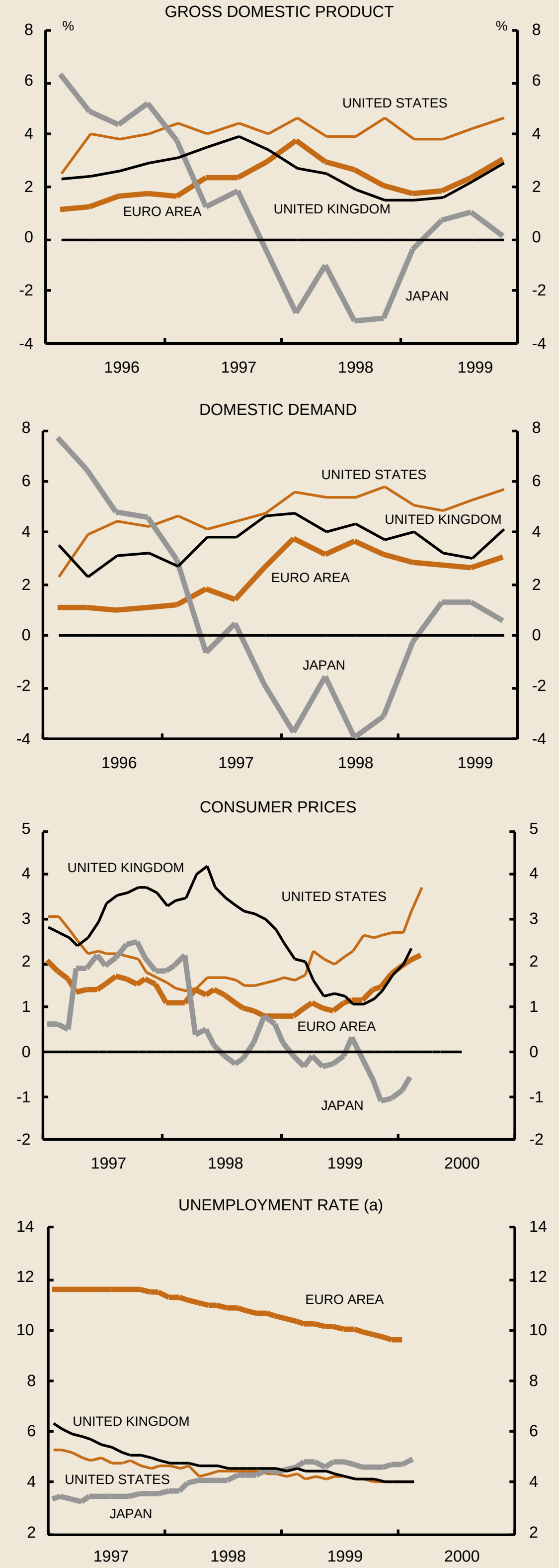
The trends observed in the final months of 1999 relating to the economic growth of the external environment of the euro area have firmed in 2000 Q1. The indicators available point to the prolongation of the robust expansion of growth in the United States, the acceleration of activity in the non-EMU EU countries and in the emerging south-east Asian economies, and the firming of the recovery in Latin America. Developments in Japan are less favourable, although there have been recent encouraging signs potentially heralding a return to positive growth rates. The generalised advance of economic activity worldwide coincides with the deterioration of the inflationary situation, essentially as a result of the rise in oil prices. Nonetheless, at the end of March, the Organisation of Petroleum Exporting Countries (OPEC) reached an agreement to increase crude oil production. That should contribute to stabilising oil prices in the coming months, although the lagged effects of past rises will continue to be felt.

According to final National Accounts data in the United States, GDP posted a growth rate of 4.6 % year-on-year in 1999 Q4 (7.3 % in annualised quarter-on-quarter terms), up three-tenths of a point on the rate for the previous quarter. This was the outcome of an additional rise in domestic demand, which offset the greater deterioration in net external demand. These figures place average growth for 1999 at 4.2 %, only one-tenth of a point below the related 1998 rate, this being the third year running in which GDP has exceeded 4 % (see Chart 5). The resilience of activity has proven compatible with the favourable trend of domestic costs, approximated by the GDP deflator, which grew by 1.5 % on average (1.2 % in 1998), despite a situation close to full employment having been attained owing to the favourable course of labour productivity. It seems increasingly difficult to attribute this pattern of growth solely to the interplay of a series of favourable economic factors and a policy mix geared to macroeconomic stability. The length of the non-inflationary growth period in the United States and the strong increase in labour productivity suggest the presence of structural changes in the economy that may be bearing favourably on its potential growth. On the evidence available, such changes might be connected with the incorporation of technical progress arising from the development of information technology and communications.

The economic indicators for 2000 Q1 point to the continuing buoyancy of demand and a further worsening of the current disequilibria. Indeed, for the first two months the consumption indicators show the continuing high growth of

CHART 5

Main macroeconomic indicators
Percentaje change on previous year



Sources: Banco de España, national statistics and Eurostat.
(a) As a percentage of the labour force.

spending, with the household saving rate at a new low (down to 0.8 % in February from an average of 1.9 % in 1999 Q4). The output indicators have also been on an expanding course, while employment has continued increasing in the first quarter of the year. The monthly wage indicators show no acceleration on recent months so unit labour costs, given the expected strong growth in productivity in 2000 Q1, remain contained. Nonetheless, consumer prices grew in March at a 12-month rate of 3.7 %, a strong acceleration on the figures for January (2.7 %) and February (3.2 %). With the fresh food and energy components stripped out, underlying inflation posted a rate of 2.4 %, also considerably up on the January and February rates of 1.8 % and 2.1 %, respectively. Lastly, the deterioration in the terms of trade continues to widen the trade deficit, which may further erode the current-account balance during the present year.

In Japan, GDP fell, for the second quarter running, in 1999 Q4 in relation to the preceding three months. This meant a year-on-year change of zero, whereby 1999 closed with average growth standing at 0.3 %, far below forecast, though clearly above the 1998 figure (–2.3 %). The economic deterioration in the second half of the year was further to the previous fiscal stimulus package having run its course, the slump in confidence (especially on the part of consumers) and the appreciation of the yen in effective terms. The only domestic demand component which trended favourably in 1999 Q4 was private investment, in line with the gradual improvement in business confidence and with the headway made in industrial restructuring. The slackness of private consumption in the last two quarters of 1999 appeared to exacerbate the adversely trending labour market in this period and the reduction of wages, though it was due above all to the persistence of deflationary expectations. The negative contribution of external demand, for its part, was largely the result of exchange rate developments.

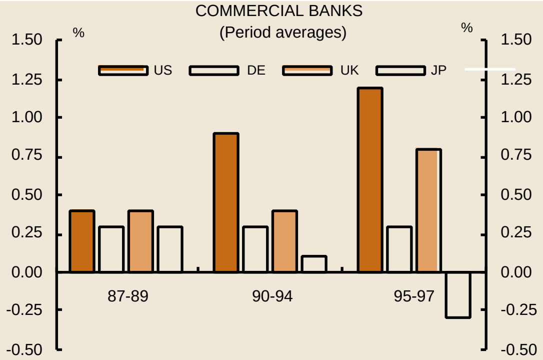
The indicators available for 2000 Q1 appear to point to an improvement in the pace of activity. Accordingly, the economic deterioration in the second half of 1999 could prove to be a transitory phase in the irregular course of the Japanese economy. Among the domestic demand components, the advance release of the household spending indicator in February suggests a pick-up in private consumption. The rise in the composite index gauging the economic climate (the Tankan business survey) in April and in the industrial production index in the first two months of the year might augur a slight recovery in private investment, which would help reinforce the expansionary effects of the latest

BOX 1

The plan for restructuring Japanese banks

Throughout the nineties, the prolonged phase of low growth and, in the main, the sharp fall in real and financial asset prices led to a heavy deterioration in the quality of Japanese banks' lending portfolios and, in particular, to the enormous growth of the volume of defaults. The consequence of this was an ongoing decline in the profitability of Japanese banks (see accompanying chart). On official estimates, non-performing loans in the banking sector accounted at the beginning of 1999 for 11.7 % of total loans, or approximately 13 % of GDP. This situation, which was compounded as from late 1997 by worsening economic circumstances, forced the authorities to refrain in 1998 from applying partial measures (as would have occurred in previous years) and to implement a comprehensive restructuring plan for the sector.

Japanese bank profitability compared (a)



Source: OECD, *Bank profitability* (1999).
(a) Profit after tax as a percentage of total assets.

The aim of this plan, devised in connection with the principles of the "big bang" financial reforms officially announced in 1997, was twofold: to prevent forthwith the possibility of the sector collapsing, and to steer to a greater extent sectoral regulations and workings towards market criteria. This involved, on one hand, a substantial reduction in the short run of the enormous volume of non-performing loans by means of a programme of government subsidies to recapitalise banks. And, on the other, the adoption of a series of legislative measures and regulatory changes designed to promote, in the medium term, greater banking profitability and solvency.

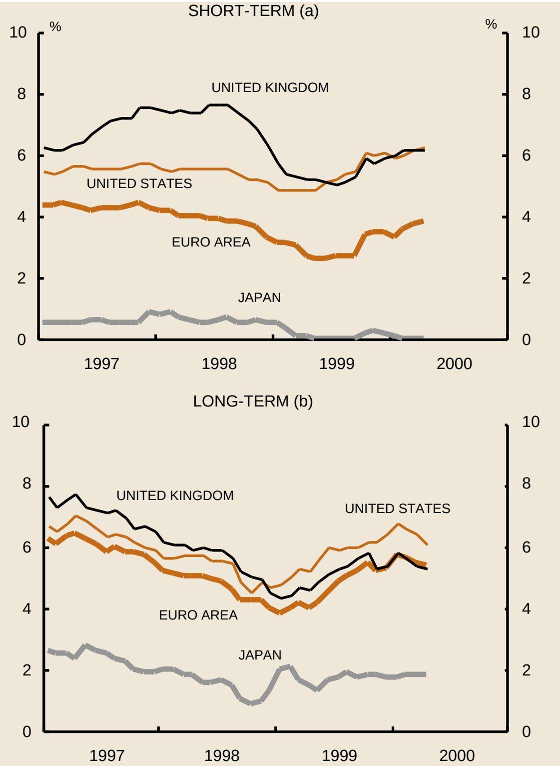
To achieve the first aim, the economic authorities gave their approval in March 1999 to public funds supplementing those granted in March 1998. These funds were aimed initially at the biggest banks and were subsequently and gradually added to in the course of 1999 as other smaller banks were targeted. The government established that the amount of the funds should be determined by the applications made by the banks themselves, requiring in exchange the submission of adjustment plans spanning four years (i.e. up to March 2003). Thus, the 15 biggest banks (with the exception of the biggest bank of all) submitted applications for government aid for a total value of JPY 7.5 trillion (1.5% of GDP). Of this amount, which was paid out in late March 1999, JPY 6.2 trillion were channelled in the form of the acquisition by the State of preferred stock, and the remaining 1.3 trillion through the purchase of subordinated debt. Banks, for their part, made two commitments in their restructuring plans. First, to remove from their balance sheets non-performing loans for a total of JPY 9 trillion (1.8% of GDP) at the end of March 1999 (the end of the financial year). And further, to implement adjustment measures which, by the end of the four years the plan covered, would bring about an estimated increase in net income of 11.5% along with declines in overhead expenses and in staffing levels of 7.9% and 11.6 %, respectively. According to certain expert assessments, the government assistance plan may be positively viewed in that it has contributed to preventing several of the biggest banks from going to the wall. Nonetheless, there are continuing doubts about whether the plan is sufficient to fully resolve the problem within the time frame and under the terms considered.

Mention should be made of the two key regulatory changes defining the new operational framework for the banking sector. Firstly, the new system set in place in April 1998 for officially classifying the risk inherent to loans extended by banks, which is more in keeping with the criteria applied internationally. And secondly, the approval in October 1998 of legislation governing financial reconstruction (which authorises the government temporarily to nationalise failing banks and to step in at banks undergoing serious difficulties) and financial normalisation (which establishes the general outline for recapitalising banks via public funds). In all, total funds of JPY 60 trillion (equivalent to 12.1 % of GDP) were made available to the Deposit Guarantee Corporation to assist banks. These funds were to be earmarked for recapitalisation, the purchase of shares via nationalisation and liquidation, and the safeguarding of the depositors in failed institutions in respective amounts of 25, 18 and 17 trillion. In addition, the Financial Reconstruction Committee was instituted as the sole banking supervisor, with reinforced supervisory powers compared with the precursor institutions.

In addition to providing a way out of the crisis, the legal amendments made have set a substantial process of change in train, with an essentially liberalising orientation. It will be focused on a banking system hitherto characterised by a high degree of government intervention. In this respect, it should further be highlighted that the economic authorities have recently indicated that the general guarantee currently in force for safeguarding bank depositors will not be prolonged beyond the date initially agreed upon (March 2001).

CHART 6

Interest rates



Source: Banco de España.

(a) Three-month interbank market interest rates. Euro area: until December 1998, weighted average of the eleven member countries; in 1999 and 2000, three-month EURIBOR.

(b) Ten-year government bond yields. Euro area: until December 1998, weighted average of the eleven member countries.

approved fiscal package on gross capital formation. Lastly, the decline in consumer prices in the early months of the year has slowed and, notably, wholesale prices in February have risen in year-on-year terms for the first time in over two years. Nonetheless, the limited leeway for expansionary demand policies and the accumulated losses in competitiveness will hinder the entrenchment of a growth path in the coming quarters. Only in the medium term, when the structural reforms undertaken begin to bear fruit, may a more sustained recovery in the Japanese economy be expected.

Turning to the non-EMU EU economies, the United Kingdom posted a GDP growth rate of 3 % year-on-year in 1999 Q4, up on the figure of 2.2 % for the preceding quarter. Average growth for the year was thus 2.1 % (2.2 % in 1998). The increase in GDP in Q4 is mainly due to the buoyancy of domestic demand, especially of private consumption, which grew by 4.5 % compared with the same period a year earlier. This was because the contribution of the external sector slipped back after three successive quarters of improvement, owing to the strength of sterling and the thrust of final demand. The indicators available for 2000 Q1 point to the continuing resilience of domestic demand, although they appear to suggest the composition of growth in Q1 will be somewhat more balanced than in the previous quarter.

As regards inflation, the retail price index excluding mortgage interest payments (used by the Bank of England to set its targets) grew at a 12-month rate of 2.2 % in February. Inflation thus held at the levels recorded since mid-1999. Nonetheless, throughout this period the differential between services and goods prices has widened, with the former growing at rates close to 4 %, far outpacing the rates of increase (of close to zero) of goods more exposed to international trade. In addition, signs of inflationary pressures have heightened since the closing months of 1999 both in the labour market, as a result of lower unemployment, and in the residential property market.

GDP in the south-east Asian zone grew in 1999 by somewhat over 4.5 %, marking a notable acceleration on the previous year. Assisting growth was the climate of stability on financial and foreign exchange markets throughout the year. The data for 1999 Q4 confirmed, in the great majority of these countries, the acceleration in activity that had begun in previous months. Output growth was very high in South Korea and Malaysia and, to a lesser extent, in Hong Kong, Singapore and China. The rest of the economies in the area affected by the 1997 crisis – the Philippines, Indonesia and Thailand – grew at rates close to 5 %.

The first signs of economic recovery were discernible in South and Central America in 1999 Q4 following the crisis beleaguering this area since mid-1998. The pick-up was assisted by the improvement in activity in the rest of the world, against a background of stable financial markets, and by the rise in price of certain commodity exports. Average GDP growth in 1999 was 0.1 %, somewhat higher than forecast, although it is the lowest rate recorded in the entire decade. On the foreign exchange markets, most currencies appreciated significantly, while on the money and debt markets, interest rates fell substantially. Stock markets in the area, however, followed differing trends. The Mexican, Brazilian and Venezuelan indices rose strongly compared with stability or slight declines in Argentina, Colombia and Chile.

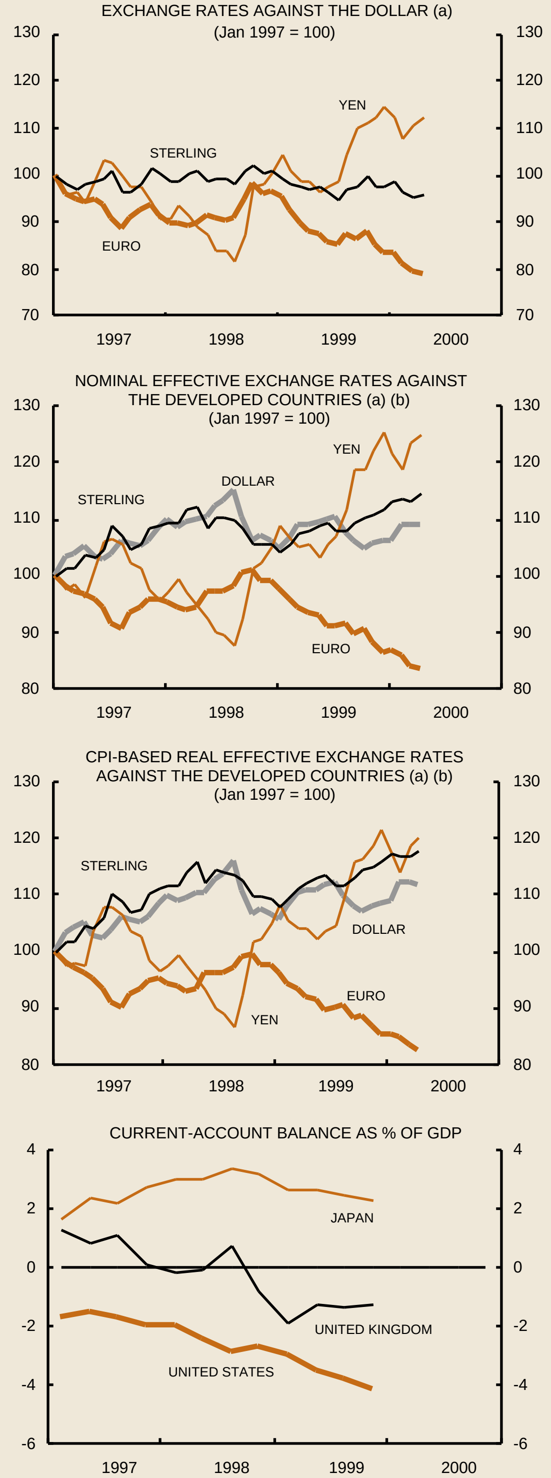
Country by country, Brazil grew 0.8 % in 1999 thanks to a strong rise in the rate of increase of GDP in Q4 (3.1 % year-on-year against –0.2 % the previous quarter). The inflation rate increased notably from July 1999 onwards, essentially as a result of the strong devaluation at the start of 1999, although this did not prevent the achievement of the target set by the Brazilian central bank for December. Nonetheless, a better inflationary outlook in the opening months of the year has allowed the monetary authority to cut its official interest rate in late March. Argentine GDP, for its part, posted a negative rate of –3 % in 1999, although it was on a clearly recovering path in the second half of the year. Mexico remained the economy in this area with the best macroeconomic results. In year-on-year terms, its GDP grew by 5.2 % in the final quarter. Despite the fact that its average inflation rate in 1999 was higher than that of the previous year, it made substantial headway in price moderation in the final months, and this has been sustained into the year 2000. The growing confidence of international investors in the Mexican economy became manifest, at the end of February, in the upgrading by credit rating agencies of Mexican government debt issues.

With respect to the economic policies of the main countries, the United States and the United Kingdom both ran fiscal surpluses in 1999, accounting for 0.5 % and 1.2 %, respectively, of GDP. These figures will probably improve in the year 2000 in the case of the United States, and the surplus will be maintained, albeit at a lower level, in the United Kingdom. In Japan, the budget deficit amounted to 7 % of GDP in 1999 and, in 2000 Q1, the latest supplementary expansionary fiscal package (JPY 18 trillion in total), implemented in the last fiscal year, has come into effect. For the current year, the recently approved budget foresees a total deficit of between 7 % and 8 % of GDP. Monetary policy in the United States and the United Kingdom has adopted in recent months a decidedly restrictive stance to counter inflationary pressures. Since the start of the year, the Federal Reserve has twice increased its federal funds rate by one quarter of a point, taking it to 6 %. The Bank of England has also twice raised its official rate, which currently stands at 6 %. Lastly, Japan continued to pursue its “zero interest rates” strategy, although the Japanese central bank has announced the possibility of abandoning this practice if the improvement in activity takes root and deflationary signs disappear.

The financial markets in the developed countries have been marked in recent months by the reduction in long-term interest rates and high stock market volatility. The rapid response by the US and UK monetary authorities to tackle inflationary pressures was favourably

CHART 7

Exchange rates and current-account balances



Sources: Banco de España, BIS and national statistics.

(a) A fall in the index denotes a depreciation of the currency against the dollar or the rest of the currencies making up the grouping, and vice versa.

(b) Before 1999 the euro is represented by an approximate indicator devised by the BIS on the basis of the effective exchange rates of the euro-area countries.

viewed on the markets, as reflected by the increase in short-term interest rates and the decline in long rates during the first quarter of the year (see Chart 6). In Japan, 10-year bond yields stabilised at around 1.8 % in February and March.

On the New York Stock Exchange, the rising trend of the technology stocks was curtailed. As a result, the NASDAQ index, which had risen from the start of the year until 9th March by 24 %, has dropped sharply since, all the more so on the release of the March inflation figures on 14th April. At the time of this bulletin going to press, the index was 34 % and 18 %, respectively, below its peak and its level at the start of the year. The more traditional securities included in the Dow Jones index, which had been volatile in the opening months of the year, also fell heavily on 14th April, placing this index around 10 % below its end-1999 level. The strong decline in the New York equity market was also immediately reflected in the Tokyo Stock Exchange Nikkei index which, in trading on 17th April, lost the gains of approximately 8 % it had built up during the year. On the foreign exchange markets, the dollar appreciated by 5.4 % against the euro and by 2.5 % against the yen in the period from December 1999 to mid-April (see Chart 7). Over the same period, sterling has appreciated in nominal and real effective terms (by 2.5 % and 1.7 %, respectively), although it has depreciated against the dollar (by 1.5 %).

3. The euro area and the monetary policy of the European Central Bank

3.1. Economic developments

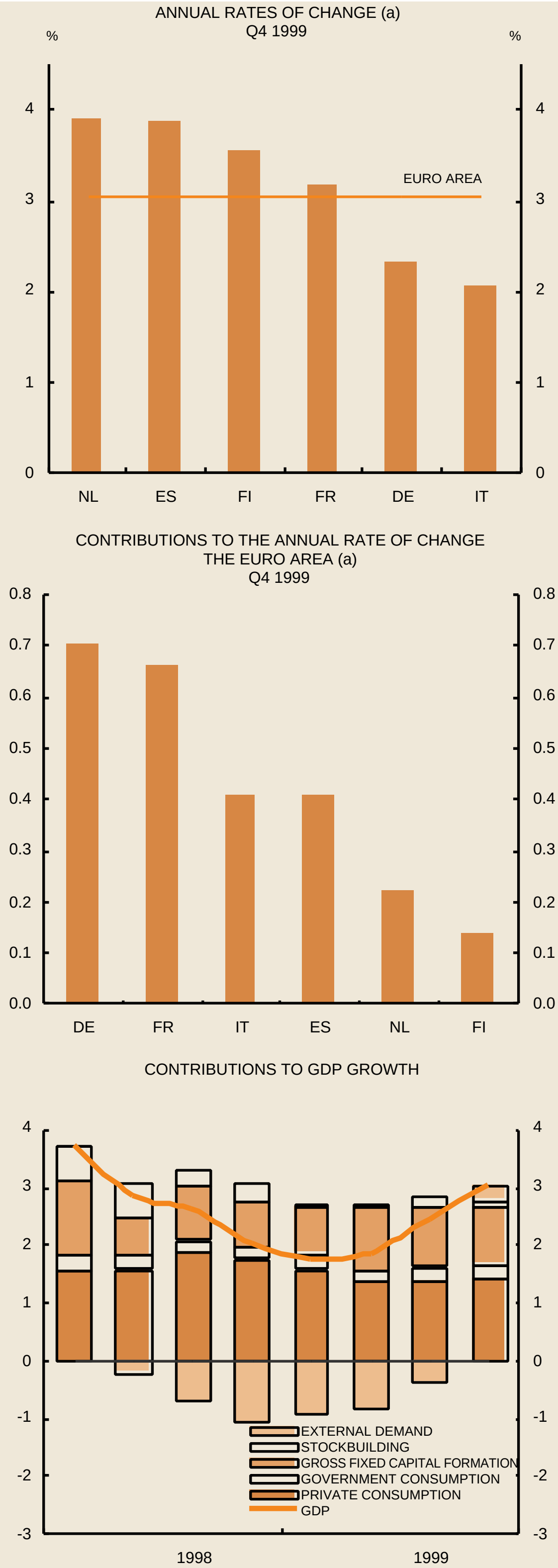
The latest data released on developments in the euro area depict a recovery led by the strengthening of net exports, the contractionary effects in recent years on the external sector of the crisis in the emerging economies having been put behind. In turn, relatively generous monetary and financial conditions and the improved climate of confidence are proving conducive to maintaining robust growth in domestic demand which, on the latest official forecasts, could be more pronounced in the coming months. Against this background, prices have continued to increase at moderate rates, albeit on a markedly quickening path as a result of the increase in the price of oil and the depreciation of the euro. Currently, the outlook for the price of crude oil and for wage costs is more favourable than it was in the previous quarter, although demand pressure and the potential emergence of second-round effects derived from the cumulative increase in the oil price pose risks to continuing price stability.

On the latest national accounts estimate for the euro area for 1999 Q4 (see Chart 8), GDP ran at a year-on-year rate of 3 %, six-tenths of a point up on the previous quarter, thereby prolonging the accelerating path dating back to 1999 Q2. The expansion of output in Q4 was underpinned by the greater contribution of net external demand (0.3 percentage points compared with –0.4 points the preceding quarter), reflecting the intense pick-up in exports. Domestic demand remained robust, increasing by 2.8 %. There was no substantial change in either its pace or its composition, since both private consumption and gross fixed capital formation trended at very similar rates to those of the two preceding quarters. Average growth for the year was 2.3 %, five-tenths of a point down on 1998 owing to the slowdown in domestic demand, since the contribution of net external demand to output was, at –0.5 percentage points, the same in both years.

Looking behind this overall pattern, the growth rates of the various economies in the area were relatively different. Countries such as Ireland and, to a lesser extent, Spain saw a higher-than-average increase in activity. This was the result of their greater potential growth, the lesser exposure of their trade to the south-east Asian economies and the greater effect of the adoption of the common monetary policy on their domestic monetary and financial conditions, as such a policy entailed nominal and real interest rates far lower than those prevailing in these countries in the period prior to the start of EMU. Germany and Italy, for their part, grew appreciably below the average owing to their

CHART 8

GDP in the euro area



Sources: Eurostat and national statistics.
(a) Excluding Belgium, Ireland, Luxembourg, Austria and Portugal, for which no quarterly national accounts data are available.

tighter trade links with the crisis-ridden economies. Further, whereas in Germany the expansionary impact of the single monetary policy has been relatively limited, Italy has borne the brunt of the forceful fiscal consolidation drive required to join EMU. Nonetheless, the course of GDP has been similar in virtually all the countries, exhibiting an upward trend throughout the year linked to the progressive recovery in exports.

The euro-area indicators for 2000 Q1 (see Chart 9) support the continuity of the trends observed in the preceding quarter, although they appear to point to a certain acceleration in domestic demand. The consumption indicators (consumer confidence, retail trade survey, new passenger vehicle registrations and retail sales) show notable signs of strength. Similarly, business surveys and indicators of activity, including most notably the industrial production index, are holding on a marked rising path.

Employment grew by 1.3 % in 1999 Q4, whereby the mild slowdown over the course of the year continued. Taking the 12 months as a whole, the average change in employment was 1.5 %, entailing a slowdown in the growth of labour productivity to 0.8 %, although in the second half of 1999 the path of recovery was patent. As regards the opening months of the current year, the unemployment rate stood at 9.5 % in February, at a similar level to the two preceding months. So far, the initial data on the outcome of collective bargaining in the year 2000 signal some restraint in wage settlements. Thus, insofar as the recovery in the growth of apparent productivity continues during 2000, following the cyclical depression in 1999, the trend of unit labour costs in the coming months could prove compatible with price stability.

On ECB estimates, the euro-area current-account balance ran a deficit of EUR 6.6 billion in January, 4.2 billion up on the same month in 1999. This was due to the sizeable decline in the merchandise surplus (EUR 0.9 billion compared with 4.8 billion in January 1999) and to an increase in the investment income account deficit, offset only partly by reductions in the deficit on services and current transfers. Underlying the increase in the merchandise deficit was the rise in the value of imports, which was greater than that in exports, owing to the forceful increase in import prices arising from higher oil prices and the weakening euro.

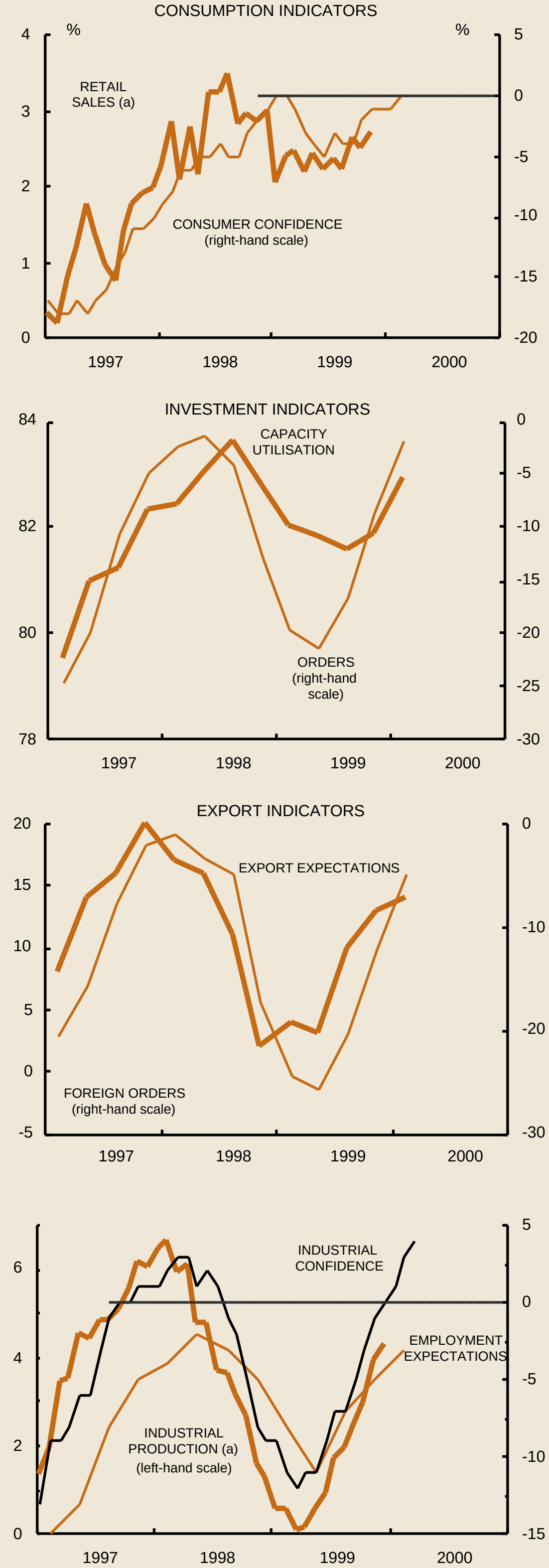
Euro-area inflation has continued to worsen in the opening months of 2000 as a result of dearer oil, the price of which grew a further 9.2 % between January and March, and the depreciation of the euro (5 % against the dollar in Q1). In March, the 12-month growth rate of the HICP stood at 2.1 % (see Chart 10), four-tenths of a point up on the December 1999 figure. This reflected the strong increase in the energy component, since the index comprising non-energy goods and services grew by only 0.9 %, a similar figure to that for the final month of last year. The trend of service prices was very stable, despite the impact of the growth of fuel prices on transport costs, against a background of more buoyant activity. Across the different euro-area member states, March saw a widening of the range in which national inflation rates are situated owing to the trend of the processed food, energy and services components. With regard to industrial prices, these grew at a 12-month rate of 5.7 % in February, six-tenths of a point up on January, furthering the acceleration discernible since last year. Component by component, the prices of intermediate goods grew by 9.2 % year-on-year, compared with 8.1 % in January, and consumer and capital goods, though still growing at moderate rates, have been following the same trend for several months.

The course of inflation in the coming months will be highly conditional upon that of oil prices, and these will largely hinge on the degree of compliance with the new supply constraints recently adopted by the OPEC countries. The OPEC members decided at the end of March to raise output by 7 %, with the aim of stabilising the price of crude oil in a range of $20-25 per barrel. Since then, oil prices have fallen by 15 % to around $22 per barrel. The increase in production, set against the seasonal reduction in demand, may suffice to stabilise the price of crude at this new level during 2000 Q2. However, if the level of compliance with the cuts were maintained close to the figure reached in February (74 %, against 91 % in July 1999), the price could fall to around $ 20 per barrel. As from Q3, the seasonal pick-up in demand could prompt a fresh increase in crude prices unless supply is once more revised upwards at the OPEC meeting scheduled for June.

With regard to budgetary policy, the decline in the overall budget deficit of the euro-area countries continued in 1999, falling to 1.2 % of GDP, eight-tenths of a point below the related 1998 figure. Nonetheless, the correction of budgetary disequilibria in 1999 was on a lesser scale than may be inferred from the course of the overall balance, since this improvement was substantially attributable to the reduction in interest payments. The primary surplus increased by only three-tenths of a point of GDP owing to the highly favourable behaviour of revenue, while current expenditure rose by 0.3 % of GDP.

CHART 9

Euro area. Real indicators

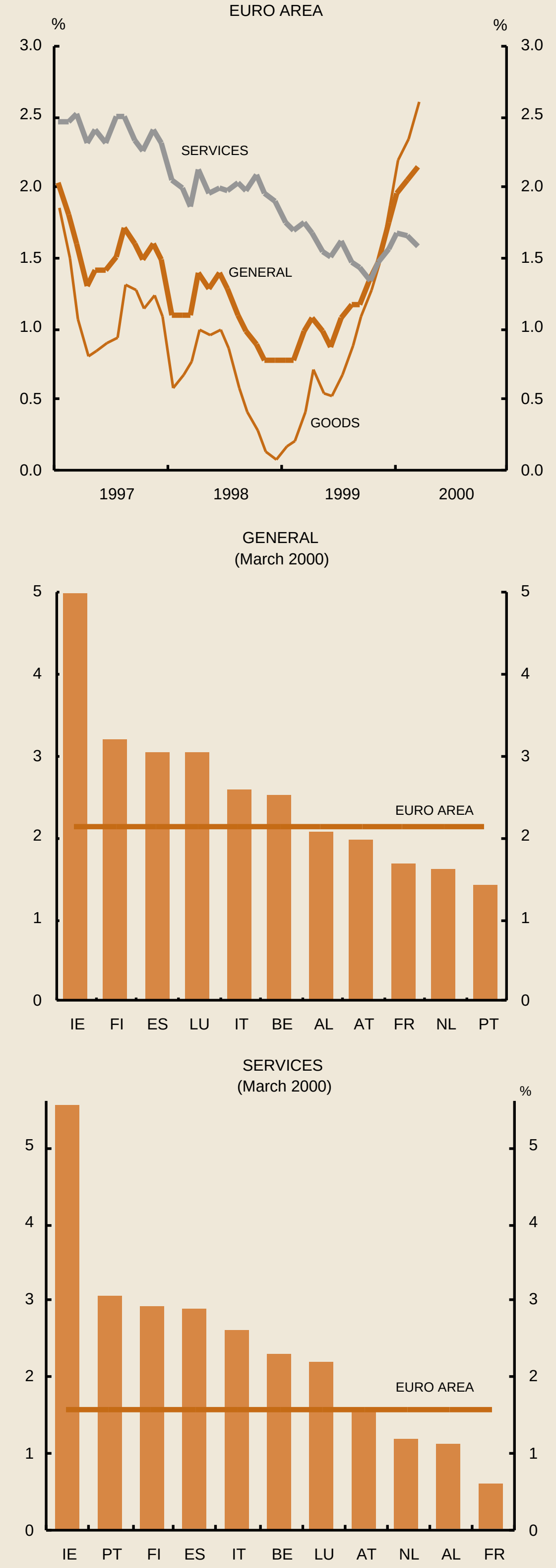


Sources: Eurostat and European Commission.

of the quarterly moving average of the seasonally adjusted series.

CHART 10

Harmonised indices of consumer prices
Twelve-month percentage change



Source: Eurostat.

Taking results country by country, none recorded a deficit in 1999 of more than 2 % of GDP and all improved their 1998 results except Ireland and Luxembourg which, nonetheless, are running comfortable surpluses. The biggest changes in the budgetary balance took place in Spain, France, Italy, the Netherlands and Finland (see Table 1).

All the euro-area countries have now submitted revised versions of their stability programmes, according to which both the deficit of the area as a whole and of each of the member states should be close to balance towards the year 2003. Among the fiscal measures unveiled in recent months are those of the French government following the upward revision, in step with the improved outlook for economic growth, of its forecast revenue for the current year. The surplus revenue will be applied only in part to reducing the deficit. The rest will be earmarked for higher expenditure on education and health (around 0.1 %) and for easing the fiscal burden, by means of a one-point cut in the main VAT rate and the lowering of income tax rates on households in the lower and middle income brackets.

3.2. Monetary and financial conditions in the euro area and in Spain

During 2000 Q1, relatively generous monetary and financial conditions have held in the euro area. In the light of the signals from other activity and price indicators, the situation has prompted growing expectations of interest-rate rises throughout the period. Indeed, the firming of more favourable growth prospects and the expansionary nature of the key monetary and financial indicators have pointed to a potential risk of inflation deteriorating in the medium term. The euro has thus continued to weaken against the dollar, compounding its significant depreciation over the course of 1999 and placing its real effective exchange rate index against the developed countries below its average level in recent years. In turn, real short-term interest rates have held at very low levels, below 2 %. Finally, the growth rates of the monetary and credit aggregates have remained high, and the latest data have shown that the most liquid components of M3 have continued to expand significantly. The combination of the foregoing factors led the ECB to raise its intervention rates on two occasions relatively close in time, on 3rd February and on 16th March. In both cases the increase was 25 basis points, whereby at the end of the period under analysis the rate on the main refinancing operations of the Eurosystem stood at 3.5 % and the rates on the marginal lending facility and the deposit fa-

TABLE 1

General government financial balance of euro-area countries (a)
(as % of GDP)

	1996	1997	1998	1999	2000 (b)
Belgium	–3.7	–2.0	–1.0	–0.9	–0.5
Germany	–3.4	–2.6	–1.7	–1.1	–1.0
Spain	–5.0	–3.2	–2.6	–1.1	–0.7
France	–4.2	–3.0	–2.7	–1.8	–1.5
Ireland	–0.6	0.8	2.1	2.0	1.7
Italy	–7.1	–2.7	–2.8	–1.9	–1.5
Luxembourg	2.7	3.6	3.2	2.4	2.6
Netherlands	–1.8	–1.2	–0.8	0.5	1.0
Austria	–3.8	–1.9	–2.5	–2.0	–1.7
Portugal	–3.8	–2.6	–2.1	–2.0	–1.5
Finland	–3.2	–1.5	1.3	2.3	4.1
MEMORANDUM ITEM:					
Euro area					
Primary balance	1.4	2.7	2.8	3.1	3.1
Total balance	–4.2	–2.6	–2.0	–1.2	–0.9
Public debt	74.7	74.5	73.1	72.3	70.5

Source: European Commission.
(a) Deficit (–) / surplus (+).
(b) Forecast.

cility at 4.5% and 2.5 %, respectively (see Chart 11).

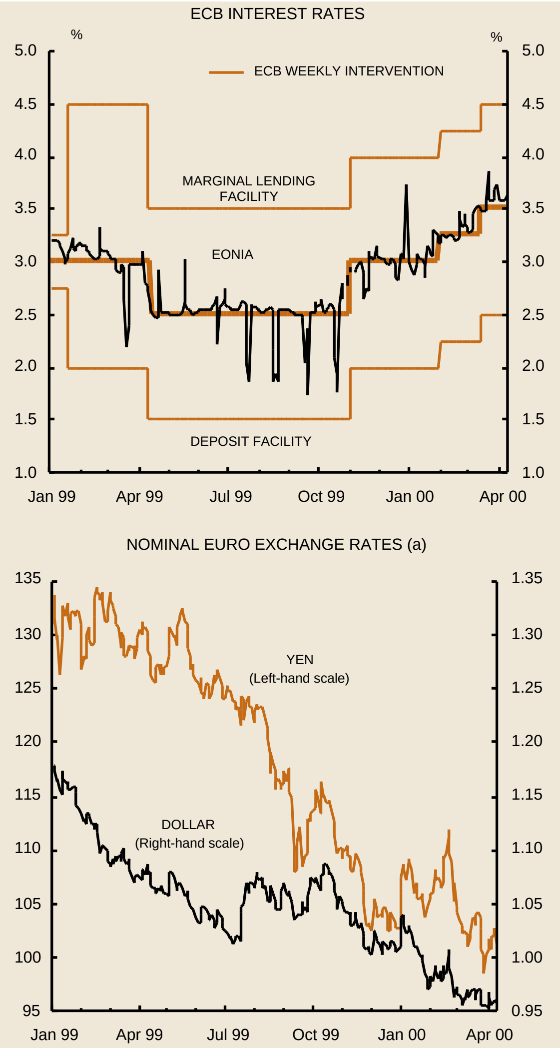
The monetary and financial situation in Spain has been more expansionary than in the euro area as a whole, and this was especially so before the ECB decided to adopt a less accommodating monetary policy stance. In particular, the most liquid financial assets and private-sector credit have been sustaining high growth rates, while the inflation differential vis-à-vis the EMU member states has meant that real short-term interest rates are lower in Spain than real rates in the euro area.

Money market interest rates in the area have trended in keeping with the hitherto prevailing expectations of an increase in the Eurosystem's intervention rates. Thus, the overnight interest rate, measured by the EONIA (European Overnight Index Average), has held above the interest rate on the main refinancing operations for much of the period and, in the run-up to tenders in which it was assumed that official rates could be raised, it stood at levels largely anticipating such movements. The rates on interbank deposits were on a similar rising trend. Indeed, by the end of the period under analysis, they stood at between 3.8 % and 4.3 % in the range from the one-month to the twelve-month maturity, respectively, between 30 and 50 basis points up on their average levels in December. In turn, rates on the futures market and implicit rates on the spot market have evidenced in this period an upward revision of the levels of short-term interest rates expected over the course of the current year. In particular, the one-month forward rate showed at the end of the period under analysis that, following the interest-rate rises by the Eurosystem, market expectations about fresh intervention-rate movements in the coming months have been sustained (see lower part of Chart 12).

In the period to date this year, the virtually continuous uptrend of interest rates on euro-area debt markets since early 1999 has been curtailed. This has been the outcome of the cushioning effect exerted by the behaviour of US markets during this period (marked by increased volatility along with a reduction in interest rates), which has checked the upward trend driven by the favourable economic growth expectations in the euro area. At the end of the period under analysis, ten-year bond yields in the euro area stood at around 5.4 %, somewhat down on the level as at end-December last year. As a result of recent developments, there has been a slight reduction in the slope of the yield curve, and the long-term yield spread over the United States has narrowed, standing in April at around 70 basis points in monthly average terms. As regards the Spanish debt markets, the behaviour of prices has run parallel to that of the main euro-area domestic markets, and the ten-year yield spread over German

CHART 11

ECB interest rates and euro exchange rates



Sources: Banco de España and European Central Bank.

(a) Dollar/euro and yen/euro exchange rate.

bunds has held at around 20 basis points (see Table 2).

Despite the reduction during this period in short- and long-term interest rate differentials between the United States and the euro area, the euro has once more depreciated against the dollar, following the trend observed since the start of 1999. In the year to date, the cumulative depreciation has been almost 5 % in monthly average terms, meaning that the nominal effective exchange rate index against the developed countries has come to stand in mid-April at more than 2 % below the average monthly level attained in December (see Chart 11).

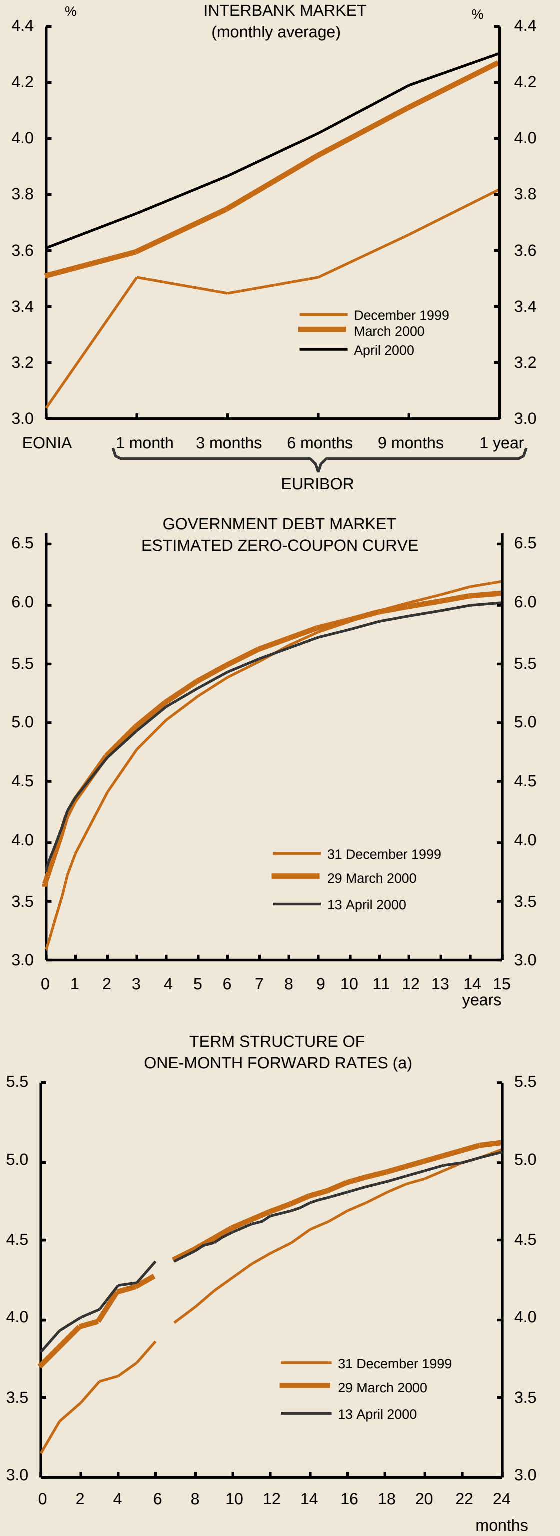
The transmission of the movements in market interest rates to the rates applied by banks in their lending and deposit operations, on an upward course since mid-1999, has continued in the first two months of the current year for which information is available. Fresh rises have thus been seen in the most representative bank rates, more significantly so in longer-term lending to firms and in mortgage loans than in shorter-dated lending (see Chart 13). As regards Spanish banks, the rates on their operations have trended similarly to those of the euro area during these two months, although the cumulative increase in lending rates since July last year has been lower than in the area as a whole, where such rates depend to a greater extent on long-term market rates.

Equity markets in the euro area have been more volatile in 2000 Q1 than in the three previous months, and the uptrend that commenced with notable force in October last year has been checked. Prices on these markets have moved against a backdrop of interest-rate increases in the euro area and high volatility on the US equity markets, where prices tended to fall. Predominant in February and in the first half of March was the influence of growing corporate profit expectations, set against the firming of the economic recovery and the restructuring of certain sectors in the euro area, especially in the telecommunications field. In mid-April, however, expectations that the Federal Reserve would tighten monetary policy prompted a sharp fall in US stock market prices, which spread rapidly to the European stock markets. That has considerably reduced the gains this year seen on the broad Dow Jones Euro Stoxx index, which includes the main European equities. In Spain, where stock markets have been more volatile than in the previous quarter and appreciated less than was the case in European markets as a whole, the fall in share prices led the Madrid General Index to slip to its end-1999 level, although it subsequently picked up to some degree.

The behaviour of the monetary and credit aggregates in the euro area was uneven in the opening months of the year, whereby the deceleration observed in January has not subsequently firmed. The latest data for February have shown high rates of expansion in the M3 monetary aggregate (its latest three-month moving average growth rate in relation to a year earlier was close to 6 %), while the buoyancy of overnight deposits has continued, with the M1 aggregate growing at a year-on-year rate above 10 %. Assessment of the figures in these opening months of the year should be made bearing in mind that the year-on-year growth of M3 was continuously above its reference rate throughout 1999, and that there was great uncertainty over the factors behind this deviation. Some of

CHART 12

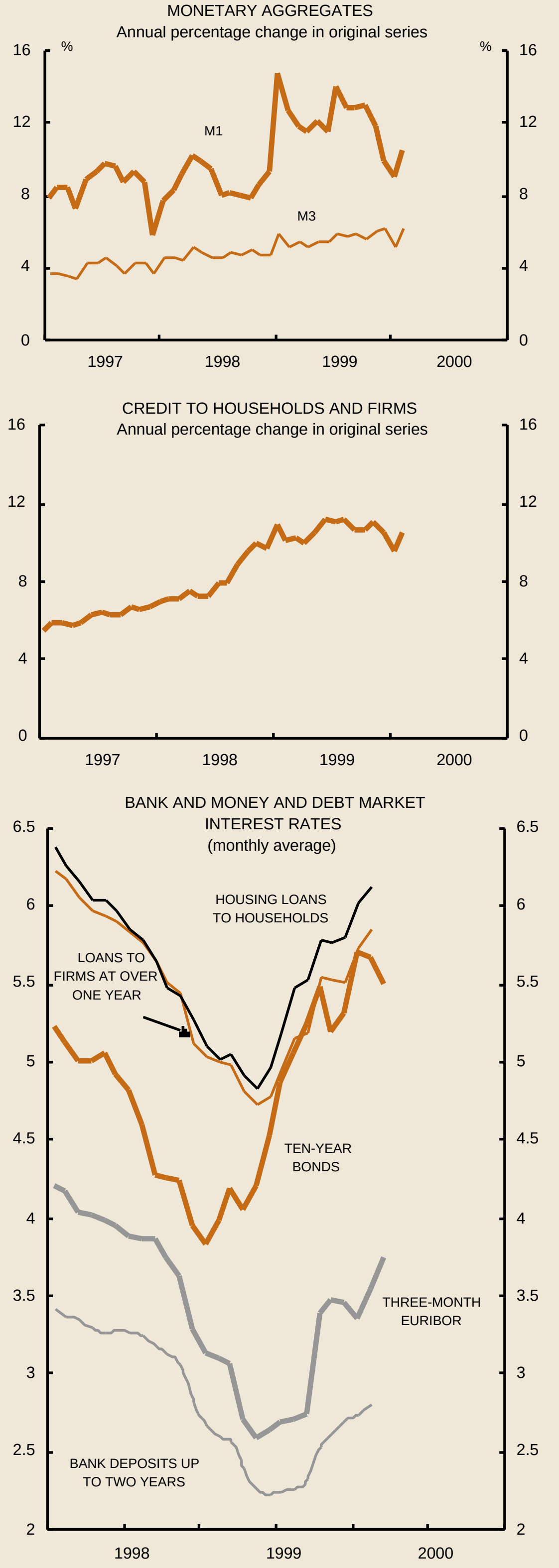
Euro area yield curves



Sources: Banco de España and European Central Bank.
(a) Implicit up to six months.

CHART 13

Monetary and credit aggregates and interest rates in the euro area



Sources: Banco de España and European Central Bank.

TABLE 2

Monetary and financial situation in the euro area and in Spain

	1999				2000			
	MAR	JUN	SEP	DEC	JAN	FEB	MAR	APR (c)
MONETARY MAGNITUDES (a):								
EURO AREA								
M3	5.4	5.5	5.9	6.2	5.2	6.2		
M1	11.7	11.5	12.8	9.8	9.0	10.4		
Credit to private sector	10.1	11.1	10.6	10.4	9.5	10.5		
SPAIN								
Liquid financial assets	4.3	4.1	4.2	3.6	2.5	2.9		
Cash and cash equivalents	15.0	17.5	17.4	11.9	10.5	12.2		
Lending to private sector	15.9	19.2	19.3	19.0	19.0	18.8		
FINANCIAL MARKETS (b):								
EONIA	2.93	2.56	2.43	3.04	3.04	3.28 %	3.51 %	3.61 %
Three-month EURIBOR	3.05	2.63	2.73	3.45	3.34	3.54 %	3.75 %	3.87 %
Government debt								
Euro-area ten-year government bond yields	*4.18*	*4.53*	*5.24*	*5.30*	*5.70*	*5.66 %*	*5.49 %*	*5.34 %*
US/euro area ten-year bond spread	*1.12*	*1.44*	*0.76*	*1.06*	*1.08*	*0.97*	*0.88*	*0.66*
Spain/Germany ten-year bond spread	*0.22*	*0.24*	*0.27*	*0.22*	*0.22*	*0.22*	*0.22*	*0.23*
Bank interest rates in Spain								
Synthetic deposit rate	*1.90 %*	*1.66 %*	*1.69 %*	*1.98 %*	*1.98 %*	*2.06 %*	*2.17 %*	
Synthetic lending rate	*5.02 %*	*4.54 %*	*4.71 %*	*5.02 %*	*5.10 %*	*5.33 %*	*5.55 %*	
Dollar/euro exchange rate	1.088	1.038	1.050	1.011	1.014	0.983	0.964	0.958
Equity market (d)								
Broad Dow Jones EURO STOXX index	*3.4*	*8.9*	*6.8*	*39.5*	*–4.1*	*6.8*	*6.0*	*3.5*
Madrid Stock Exchange General Index	*–0.1*	*4.2*	*–1.2*	*16.2*	*–3.4*	*11.4*	*7.5*	*2.9*

Sources: European Central Bank and Banco de España.

(a) Percentage change on a year earlier.
(b) Monthly averages.
(c) Average for the month up to the latest information available.
(d) Month-end data. Latest data available: 14 April 2000.

the momentum of this growth might have been associated in the opening months of 1999 with certain special effects arising from the introduction of the euro and the start-up of Monetary Union, which might have increased the demand for overnight deposits. However, the persistently high growth rate of M3 in subsequent months and the recent downward stickiness of its growth rates suggest that the pattern of behaviour of this monetary aggregate has been due not so much to special factors but, above all, to a genuine process of liquidity expansion.

In Spain, analysis of the variables allowing an assessment of the liquidity conditions of the Spanish economy reveals, as in the case of the European monetary aggregate, the considerable buoyancy of the more liquid assets. Cash and cash equivalents (which include cash in circulation, overnight deposits and savings deposits), having trended downwards since 1999 Q4, have expanded significantly in February at a year-on-year growth rate of around 12 %. Deposits with an agreed maturity have also shown increasingly marked vigour. However, the sharp fall in shares in securities funds during these first two months of the year has meant that the growth rate of liquid financial assets as a whole has decelerated to below 3 % year-on-year in February (see Table 2).

Turning to the credit aggregates, finance extended by Monetary Financial Institutions to euro-area residents expanded in February at a rate similar to that observed over the course of 1999, at around 8% in year-on-year terms. This overall figure was a result of differing performances across the various sectors. Compared with the restraint of lending to general government, which grew by 1 % year-on-year in February, finance to the private sector, after having slowed in January, once more proved as vigorous as it had in 1999, running at a growth rate of over 10%. The net external position of MFIs continued to diminish over the first two months as a result of a bigger increase in liabilities vis-à-vis the external sector than in foreign assets; it was EUR 123 billion lower in February than in the same month a year earlier. As indicated in previous reports, this gap is providing for a faster growth rate of credit than of liabilities vis-à-vis euro-area residents.

The growth rates of the representative credit aggregates in Spain have remained high, against a backdrop of economic expansion and favourable finance conditions. The latest data on finance to the resident private sector (non-financial corporationand households) show its growth rate to be holding at around 19 %, unchanged since mid-1999. This is the result of something of an acceleration in the finance raised by a companies, which is growing at over 20 %, and of mild restraint in credit to households. The growth rate of finance to general government has grown slightly at the start of this year, although a partial influence here has been the specific course of the State deficit in the early months of the year 2000. In any event, the following section of this "Quarterly Report" offers a more detailed analysis of financial flows in the main sectors of the Spanish economy.

4. The Spanish economy

The Spanish economy benefited last year from the general global economic upturn and, in particular, from the expansionary effect it had on euro-area activity in the second half of the year. The rate of growth of activity in Spain, which had been adversely affected by the international economic crisis in late 1998 and early 1999, was back on an upward trend, reaching 3.9 % year-on-year in Q4. Throughout the period, domestic demand sustained high growth rates (albeit with a moderate downward trend), based on loose monetary and financial conditions (as described in the preceding section), and on a fiscal stance that combined a strong increase in tax receipts with measures encouraging spending by other sectors. From the information available on activity and demand in the first quarter of 2000 it appears that the recovery in output continued, led by a further improvement in net external demand, while domestic demand grew at a real year-on-year rate of around 4.5 %, close to its end-1999 level.

As in other European economies, the Spanish inflation rate ended 1999 on a rising trend, owing to the increase in energy prices. In the first quarter of the year 2000 prices continued to grow at high rates, which can be expected to dip as the oil price returns to more moderate levels. The inflation differential with the euro area, having remained at around one percentage point in 1999, fell by a few tenths of a point at the beginning of 2000. In any event, wages continued to help moderate prices, ensuring not only that the inflation rate did not accelerate further, but also that employment creation was high in 1999 and, on the available information, is still high now.

4.1. Demand

On Quarterly National Accounts (QNA) estimates, national demand grew in 1999 Q4 at the high real year-on-year rate of 4.2 % (1). This was, nonetheless, below the rates of close to 5 % estimated in preceding quarters (see Chart 14) as a consequence of a levelling off in the rates of growth of all the spending components. In the final quarter of the year, the growth rates of household and general government final consumption spending and of gross fixed capital formation in relation to capital goods and construction appear to have slowed. Despite the loss of momentum of national demand, GDP accelerated slightly, to reach a real year-on-year rate of 3.9 %, since the negative

(1) The QNA figures referred to in this chapter are defined in trend-cycle terms, in accordance with the terminology used by the National Statistics Institute.

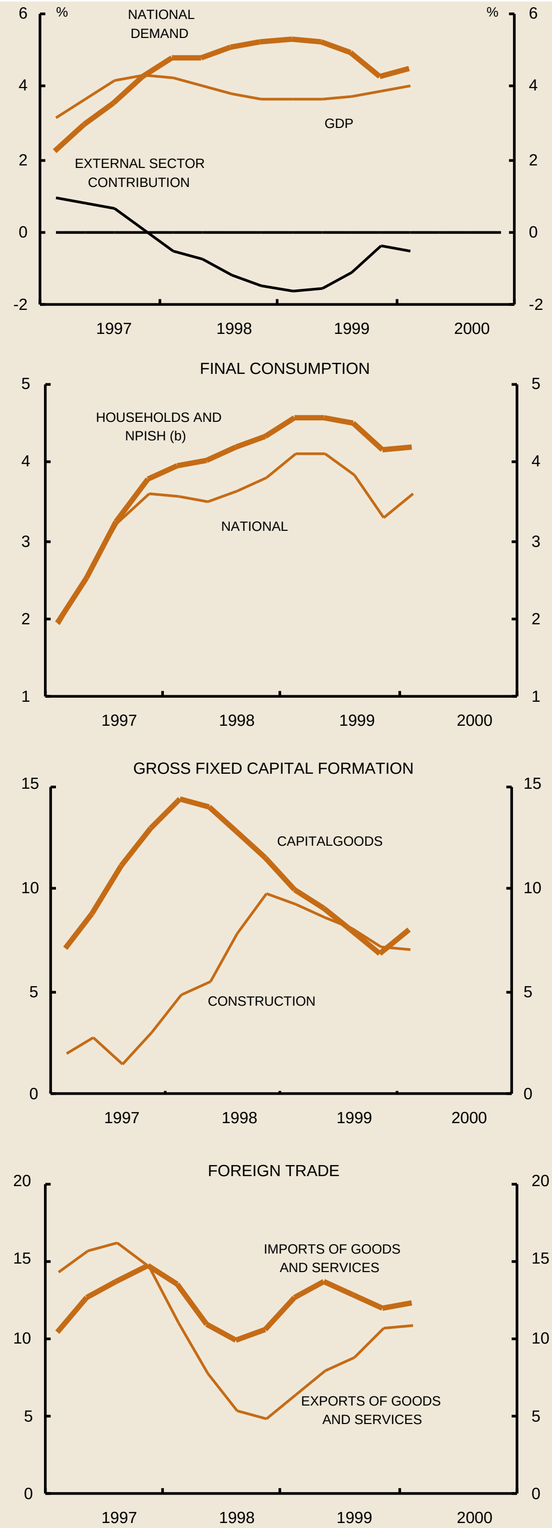
contribution of net external demand to output growth fell significantly, to stand at –0.4 percentage points, down from –1.1 points in Q3. This outcome was due to the greater buoyancy of exports, which rose by 10.7 % in Q4, two percentage points more than in Q3, and to lower import growth, although the latter was still running at a rate of 11.7 %.

Following the release of the INE estimates discussed above, further information on end-1999 has been received. Overall, this seems to indicate that the slowdown in national demand in Q4 may have been less pronounced than originally estimated, while the contribution of net external demand would have been somewhat more contractionary. The short-term indicators for the first quarter of 2000 – based on very incomplete data – suggest that domestic demand continued to grow at high rates of close to 4.5 %. Household final consumption spending would have grown in the first quarter at similar rates to those in the preceding quarter, investment in capital goods would have gained momentum and the slowdown in construction spending, dating back to 1999 Q1, may have diminished. As regards foreign trade flows, goods exports continued to recover while imports stabilised at a high rate of growth, indicating a less contractionary contribution from net external demand than in 1999. Overall, GDP may have risen in the first quarter of the year at a year-on-year rate of 4 %, slightly up on the previous quarter.

On QNA data, household final consumption expenditure grew in 1999 Q4 by 4.2 % year-on a-year, in real terms, three-tenths of a percentage point less than in the preceding quarter. This slowdown has been captured by some indicators, such as apparent consumption of goods and new car registrations, while other indicators, such as the retail sales index and total household spending, estimated by the Spanish Household Expenditure Survey, show more sustained growth, more in line with the recovery in the consumer confidence index in that period (see Chart 15). In fact, the scant information available on consumption in 2000 Q1 would indicate that the slowdown in its growth came to a halt, a fact that would also be consistent with the high levels of consumer confidence in the first quarter. The retail sales indicator, deflated by consumer prices, grew by 9.5 % year-on-year in January and February, well above the Q4 rate of 4.5 %. New car registrations grew strongly in the same months, and although they were weak in March this may have been linked to the timing of Easter. In any event, the growth rates of consumption of consumer durables, according to the relevant apparent-consumption index, would have levelled off. Finally, although

CHART 14

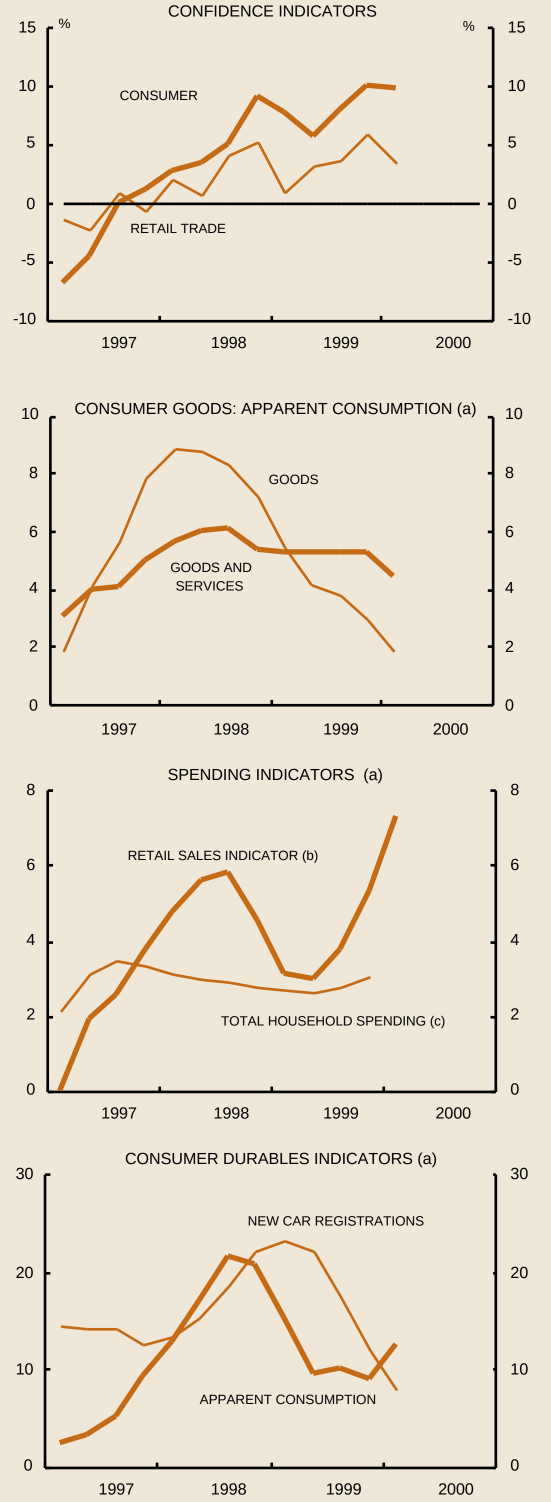
Main macroeconomic aggregates (a)



Sources: Instituto Nacional de Estadística and Banco de España.
(a) Non-centred annual percentage change, based on the trend-cycle component.
(b) Non-profit institutions serving households.

CHART 15

Private consumption indicators



Sources: Instituto Nacional de Estadística, European Commission, Dirección General de Tráfico and Banco de España.

(a) Non-centred annual percentage change, based on the trend of the indicator.

(b) Deflated by the CPI.

(c) Household expenditure survey, deflated by the CPI.

on the basis of incomplete information for the first quarter the ongoing slowdown in the aggregate indicator of apparent consumption of consumer goods seems to have continued, this was due to the poor performance of the food component, since other consumer goods grew at similar rates to those in the fourth quarter.

The strength of household consumption in 2000 Q1 is based on the positive performance of its main determinants. Indeed, it is estimated that household disposable income will rise in the year as a whole at a rate similar to that in 1999. As regards the compensation of wage earners, the slight slowdown in employment will be offset by the higher growth in average compensation. The payments arising from the triggering of inflation-adjustment clauses in 1999 settlements received in the first quarter of the current year will have contributed to this higher growth. Net transfers from the public sector will also help to sustain disposable income. The social benefits received by households have been boosted by the increases in pensions stemming from the rise in the minimum pension and from the compensation for the inflation overshooting in 1999, partly replacing the expansionary impulse provided by the reform of personal income tax last year. The relatively expansionary performance of disposable income is supplemented by the improvement in household expectations and the rise in property values, factors conducive to consumption rising faster than income. As already mentioned, the consumer confidence index improved significantly in February and March, regaining levels close to its all-time high, helped by the rapid reduction in the rate of unemployment. In addition, financial conditions remain favourable for the expansion of household expenditure.

In 1999, on QNA data, general government final consumption spending grew by 1.8 %, in real terms, with a profile of progressive slowdown over the year. The information available for the first quarter of 2000, relating exclusively to the State, is distorted by the transfers of responsibilities to the regional (autonomous) governments. However, it is estimated on the basis of the budget plans for the current year that the trend slowdown in general government final consumption expenditure will come to a halt, so that the rise in this expenditure will be similar to that in 1999 as a whole.

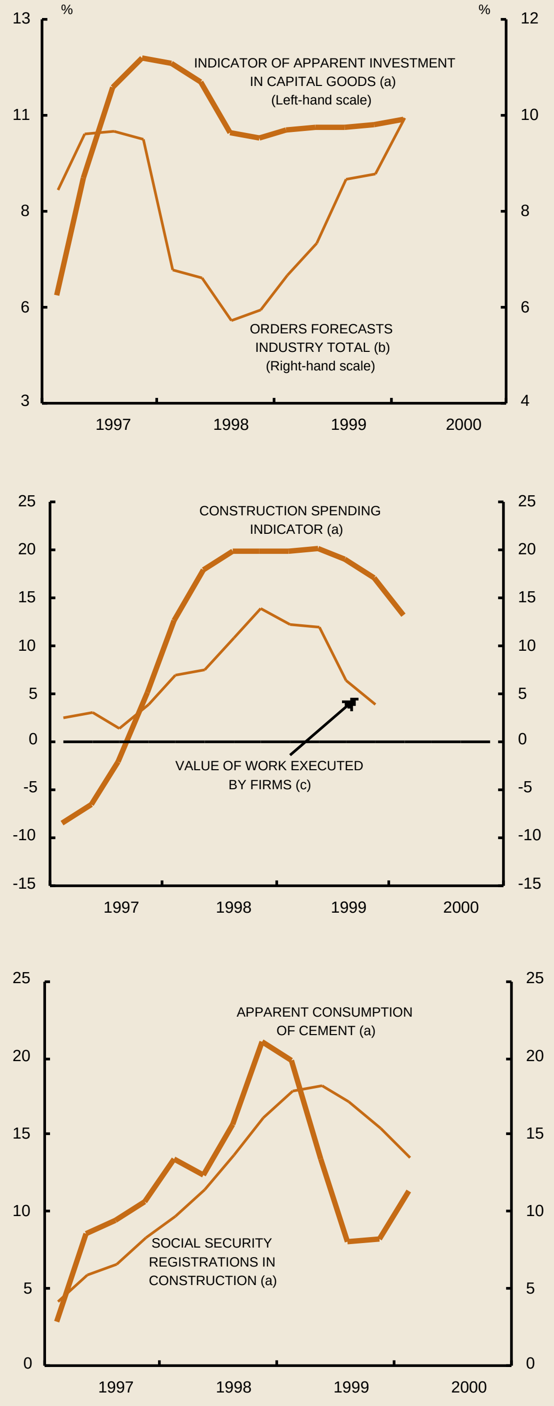
In 1999 Q4, on QNA estimates, the slowdown in gross fixed capital formation that commenced in preceding quarters accelerated, reducing the real year-on-year growth rate to 7 %, one percentage point less than in Q3. The diminished buoyancy of investment was a result of weakness in both construction spending and in investment in capital goods. Investment in capital goods grew, on QNA estimates, at 6.8 % year-on-year, in real terms, somewhat more than one percentage point less than in the third quarter and significantly below the 10 % rate of the first quarter of the year. It should be noted though that the information available for end-1999, in particular that provided by the apparent investment indicator, based on full information for the year in question, seems to suggest that the slowdown in this spending component last year may have been less sharp (see Chart 16). This has given rise to an estimate for year-on-year growth of close to 8 % for investment in capital goods in 2000 Q1, in line with the growth signalled by the apparent investment indicator for this period (albeit based on incomplete data). It should be noted that the latest figures for the industrial production of capital goods, relating to February, show a recovery, although the business survey run by the Ministry of Industry and Energy, on data to February, has tended to indicate a somewhat less optimistic situation in investment goods industries. Meanwhile, the autumn results of the weekly investment survey of industrial firms signal, besides an upward revision to investment in 1999, investment growth in the year 2000 at very close to the 1999 rate, in nominal terms.

In general, the buoyancy of spending on capital goods forecast for the beginning of 2000 is in line with the expansionary behaviour of final demand and with the expectation that this strength will be sustained in the coming quarters. In fact, industrial orders, a variable approximating expected demand, have been markedly expansionary since end-1998, as seen in Chart 16. Moreover, the financial position of firms, reflected in the results of the Central Balance Sheet Office quarterly survey (CBQ) available to 1999 Q4, remains very comfortable, with low levels of indebtedness and a very high return on assets. Given that the cost of borrowing continued to fall to the end of 1999, the differential between this cost and profitability continues to widen, which is in principle conducive to new investment.

Construction investment remained highly buoyant in 1999 Q4, growing by 7.1 % year-on-year, although the slowdown to which it had been subject during the year became more pronounced. In any case, in 1999 as a whole, the growth of construction investment was notable, due to the healthy performance of building, while civil engineering works began to show signs of stagnation as from the second half of the year. Within building, the growth in residential investment, against a background of growth in employment and disposable income and low interest rates, which boosted the demand for

CHART 16

Gross fixed capital formation indicators



Sources: Instituto Nacional de Estadística, Ministerio de Industria y Energía, Ministerio de Fomento, OFICEMEN, Instituto Nacional de Empleo and Banco de España.

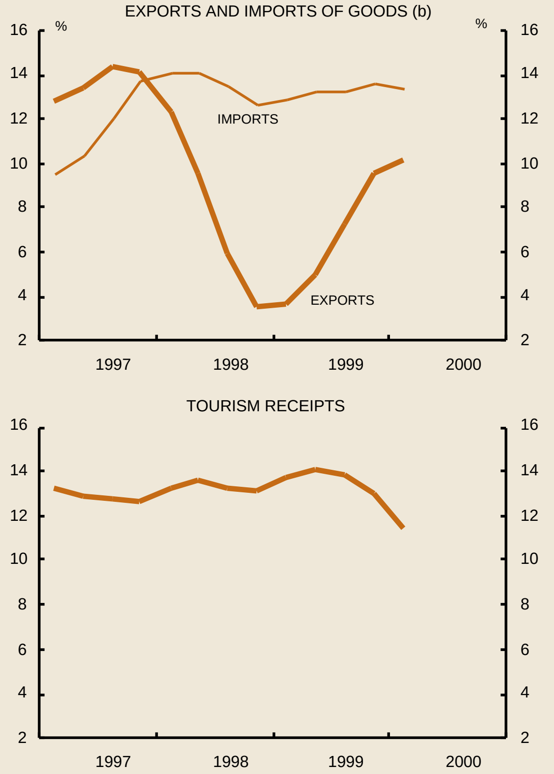
(a) Non-centred percentage change on same quarter a year earlier, based on the trend of the indicator.

(b) Trend level.

(c) Obtained from the quarterly construction industry survey and deflated by the construction costs indicator. Four-quarter rate of change based on original series.

CHART 17

Foreign trade (a)



Sources: Ministerio de Economía y Hacienda, and Banco de España.

(a) Non centred percentage change on same quarter a year earlier, based on the trend of the indicator.

(b) Series deflated by the related unit value indices.

dwellings, was notable. Also, the healthy financial position of firms helped to boost spending on non-residential building.

The most recent short-term information, relating to the first quarter of the current year, seems to indicate that the slowdown in construction was tending to be curbed in this period. Input indicators, such as the index of industrial production of construction materials and apparent consumption of cement, have signalled greater buoyancy in the most recent months, which could be related to the onset of a period of greater buoyancy in civil engineering, which uses such materials very intensively in the early stages of work (see Chart 16). However, the indicators of employment in the sector show a continuation in the first quarter of the year of the slowdown displayed since the second half of the previous year. From a medium-term viewpoint, the recent behaviour of the leading indicators implies a further slowdown in this component of investment in the coming quarters. The rate of growth of indicators of new building starts in the private sector fell in the second half of 1999 and the volume of work tendered by general government dropped in 1999 as a whole, although the decline was less pronounced in the last few months of the year.

To finish off the components of gross capital formation, it should be noted that, as in the two preceding quarters, stockbuilding added one-tenth of a point to the year-on-year growth rate of GDP in 1999 Q4. The scant information available for 2000 Q1 comes from the business survey and seems to indicate a certain rise in the level of stocks in industry.

As mentioned at the beginning of this section, provisional QNA estimates indicate that the negative contribution of net external demand to output growth fell significantly in 1999 Q4, to stand at –0.4 percentage points, down from –1.1 points in Q3 and –1.5 points in the first half of 1999. This smaller deterioration in the external imbalance was a consequence of the strong recovery in exports in the final quarter and the slight slowdown in imports, which nonetheless continued to grow at high rates. The figures for December goods trade, which were not known at the time the QNA estimates were released, confirm that net external demand made a smaller negative contribution to GDP growth in Q4. However, they seem to indicate that the correction was less significant than initially estimated by INE. These figures show that exports accelerated significantly in the final quarter of 1999, driven by the strong improvement in the global economy and by the euro's depreciation against the US dollar, but they also show that imports were highly buoyant too, growing at even higher rates than in Q3. The still very scant information on the first quarter of 2000 indicates that the recovery in world trade and the ongoing depreciation of the euro against the US dollar continued to strengthen exports, while imports sustained a high rate of growth, driven by the growth in final demand and the pick-up in industrial production.

Goods exports were on an upswing throughout 1999. This firmed in Q3, with the improvement in the European economies and the recovery in Asian markets, and strengthened in Q4, with the upturn spreading to all Spanish export markets. In the latter period, exports reached a real year-on-year growth rate of 10.3 %. January 2000 customs figures show that the upswing extended into the beginning of the current year, as a result of the expansionary behaviour of sales to the EU and the strong growth in those to other markets (see Chart 17). As regards product types, the ongoing robust growth in capital goods, against a background of heavy price falls is notable, as is the buoyancy of sales of non-energy intermediate goods, driven by the recovery in global activity. Sales of non-food consumer goods gained new momentum, owing to the growth in semi-manufactures and cars, while exports of food consumer goods grew more moderately. As regards the performance of service exports, tourism receipts displayed considerable strength in 1999, surpassing the excellent results of the previous year. The progressive improvement in the European economies, where most of the tourists visiting Spain come from, and the recovery in the countries afflicted by the international crisis, together with the euro's depreciation against the US dollar and against sterling, were responsible for this very positive performance by tourism. The only data available for the year 2000, referring to January, shows a slowdown in tourism receipts from the very high end-1999 rates. Finally, non-tourism services were very buoyant during 1999, the receipts associated with financial services, insurance and information technology services being particularly dynamic.

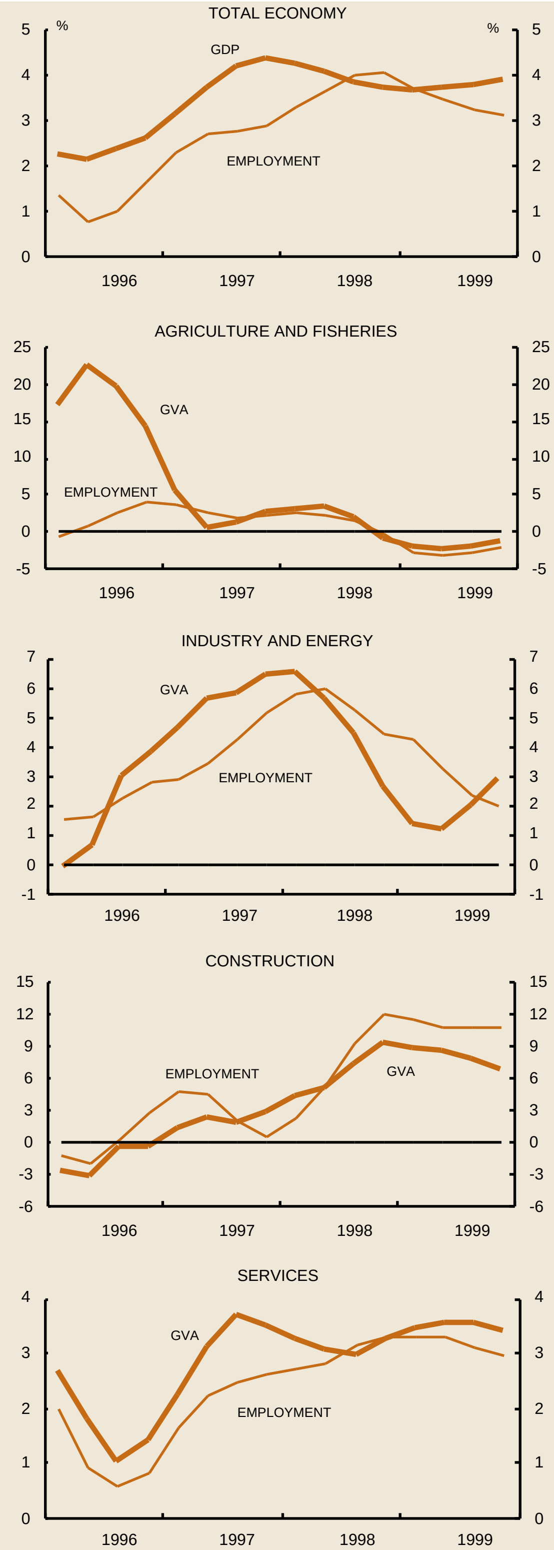
Goods imports grew at notably high real rates – well above those for exports – during 1999, as a consequence of the firm growth in final demand. However, a mild slowdown began in Q3 and, on QNA estimates, continued in Q4, with the year-on-year growth rate down to 11.7 % in the latter period. As mentioned above, complete customs data for 1999 Q4 would seem to indicate a strengthening of imports, in line with the recovery in final demand. The information available on January suggests that the high real growth rates of foreign purchases levelled off, against a background of sharp rises in prices. That said, given the volatility of these flows, further data will be required to corroborate this development. As regards groups of products, energy imports were particularly vigorous in January, while the rate of growth of non-energy components slowed, especially imports of capital goods and non-food consumer goods. Finally, service imports grew at a high rate in 1999. Tourism payments accelerated significantly in the second half of the year, to reach a real growth rate well up on that of the previous year, reflecting the high level of consumer confidence. This strong rate of growth moderated in January 2000. Non-tourism payments were also buoyant in 1999, especially those relating to financial services, in tune with the strong foreign investment activity generated during the year.

4.2. Output and employment

From the viewpoint of the productive branches, the slight acceleration of GDP in 1999 Q4 -

CHART 18

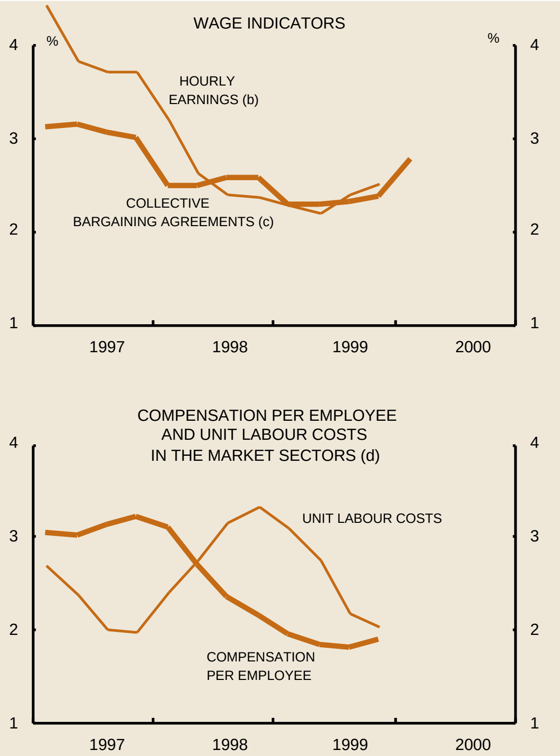
Gross value added and employment by industry (a)



Sources: Instituto Nacional de Estadística and Banco de España.
(a) Non-centred percentage change on same quarter a year earlier, based on the trend-cycle series published by the INE. Employment refers to full-time equivalent jobs.

CHART 19

Wages and labour costs (a)



Sources: Instituto Nacional de Estadística and Ministerio de Trabajo y Asuntos Sociales.
(a) Percentage change on same quarter a year earlier.
(b) Basic pay.
(c) Average settlement for the year to date, without taking into account inflation-adjustment clauses.
(d) Rates based on QNA trend-cycle series.

from 3.8 % to 3.9 %, year-on-year – stemmed from increased buoyancy of the industrial branches and a smaller negative contribution by agriculture to output growth. At the same time market services grew at a higher rate, while construction saw moderation in its growth rate, while continuing to be the most expansionary activity (see Chart 18). These trends continued in the first quarter of the current year, according to the short-term information available, with a further acceleration in GDP estimated. Against this background, employment generation continued to display notable strength. The number of full-time equivalent jobs rose by 3.2 % in 1999 Q4, with respect to the same period a year earlier, similar to the rate estimated for Q3. This stable employment growth enabled apparent labour productivity to continue to recover, to reach a year-on-year rate of 0.7 %, which is nonetheless still somewhat low compared to the average for the last decade. The recovery in productivity was especially notable in industry, where employment growth slowed. In the first few months or 2000, the employment indicators have continued to display notable strength, although it is estimated that the rate of growth has been slightly below that in the second half of 1999, enabling apparent labour productivity to recover further.

In 1999 Q4, real gross value added in agriculture fell by 1.3 % year-on-year, almost one percentage point less than in the preceding quarter. The decline in arable production was a result of the low rainfall in Spain last year, although the fact that the unfavourable weather conditions did not affect all regions equally explains why the output of some crops, such as vegetables and especially fruit, increased. The growth in the output of animal products partly offset the sharp fall in arable output; the production of meat, milk and eggs showed greater vigour. The lack of rain in the first quarter of 2000 gave rise to a potentially unfavourable scenario for agricultural production this year, which seems to have changed in recent weeks.

In the last few months of 1999, industrial activity received the stimulus arising from the progressive recovery of the European, South American and Asian economies, as well as from the prolonged expansion of the US economy, against a backdrop of depreciation of the euro. Industrial gross value added rose by 2.9 % in Q4, with respect to the same period a year earlier, nine-tenths of a percentage point more than in Q3. The most recent economic information is unanimous in signalling a continuation of accelerated growth in industrial value added. In February, as in previous months, the index of industrial production was expansionary, reaching a year-on-year growth rate of 10.2 %, which took its trend growth rate close to 5 %. Also, industrial social security registrations recovered significantly in 2000 Q1, increasing by 3.8 % year-on-year, as against 3.1 % in 1999 Q4. The results of the surveys of industrial employers' confidence have moved in the same direction; the business confidence indicator was three percentage points higher in March than in December, with an improvement in expectations regarding output and orders. At the level of the individual industries, it can be seen that the expansion of industrial activity was fairly broad based in the most recent period, although the slowdown in other manufacturing industries sounds a discordant note.

As was implicit when analysing investment in construction, activity in this industry continued to be highly buoyant in 1999 Q4, although it slowed from the previous quarter to a real year-on-year growth rate of 6.9 %. According to the preliminary results of the quarterly construction industry survey, the reduced momentum of activity in Q4 was apparent in both civil engineering and building, although the loss of vigour in the former was much greater. Some of the coincident indicators for construction activity, mainly relating to trends in inputs, have tended to show a levelling off of their deceleration in 2000 Q1.

Value added in services decelerated slightly in 1999 Q4. Its year-on-year growth rate fell to 3.4 %, one-tenth of a point lower than in Q3. This loss of momentum stemmed from non-market services, which decelerated by eight-tenths of a percentage point, while market services sustained their trend of mild acceleration, to reach a growth rate of 4.4 %. This expansion was not across-the-board, but was concentrated in telecommunications and, to a lesser extent, in corporate, personal and air-transport services. The scant economic information available on the first quarter of the current year shows a recovery in the distributive trade, accompanied by a loss of momentum in hotels and restaurants.

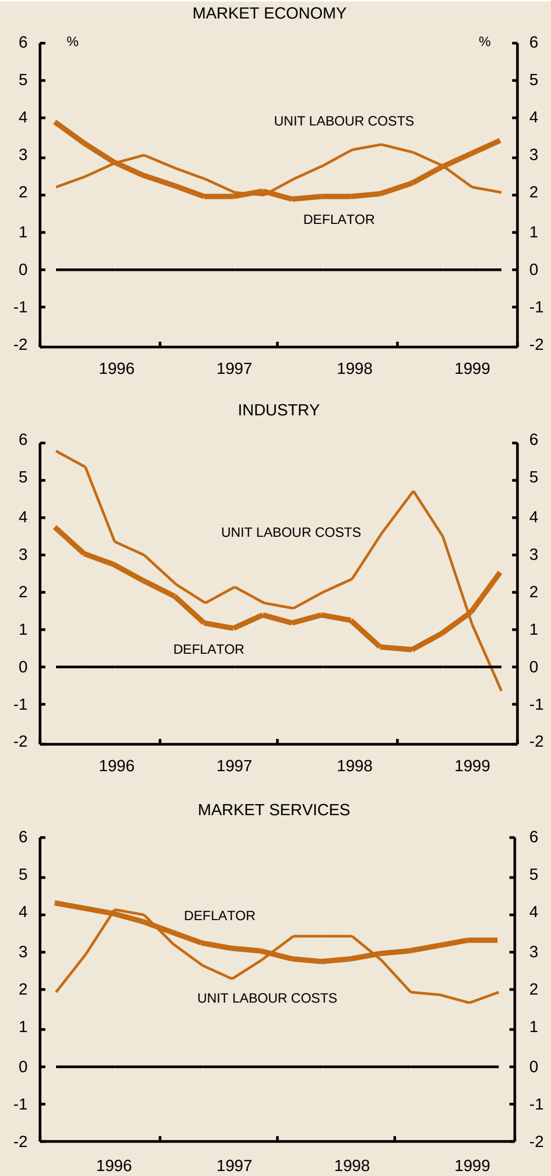
As mentioned above, the QNA data confirm that the Spanish economy continued to generate employment at a very brisk rate in 1999 Q4. In terms of full-time equivalent jobs, a variable which measures employment in terms of standardised working hours, employment grew by 3.2 % on the same period a year earlier, enabling apparent labour productivity to recover (see Chart 18). Those indicators offering information on the first few months of the year 2000 show that the rate of employment growth – albeit still vigorous – was slightly down on end-1999, and the recovery in productivity will have continued in this period. Specifically, the number of social security registrations rose by 5.4 % in 2000 Q1, entailing a moderate slowdown from 1999 Q 4.

Industry by industry, employment growth in 1999 Q4 was, in relative terms, in line with the differences in output buoyancy. In construction and services the year-on-year rates of growth were higher (11 % and 3 %, respectively, on QNA data) than in industry (1.9 %), while employment continued to decline in agriculture. As a result, with the exception of non-market services, apparent labour productivity recovered in all industries. According to the information on social security registrations, employment in 2000 Q1 continued to grow at high rates in construction and in market services, albeit with a mild slowdown, while it recovered in industry.

Net job creation was concentrated among wage-earners, as self-employment tended to decline. This feature is common to the QNA and the Labour Force Survey (EPA) data. As mentioned in previous reports, the information

CHART 20

Prices and costs by industry (a)

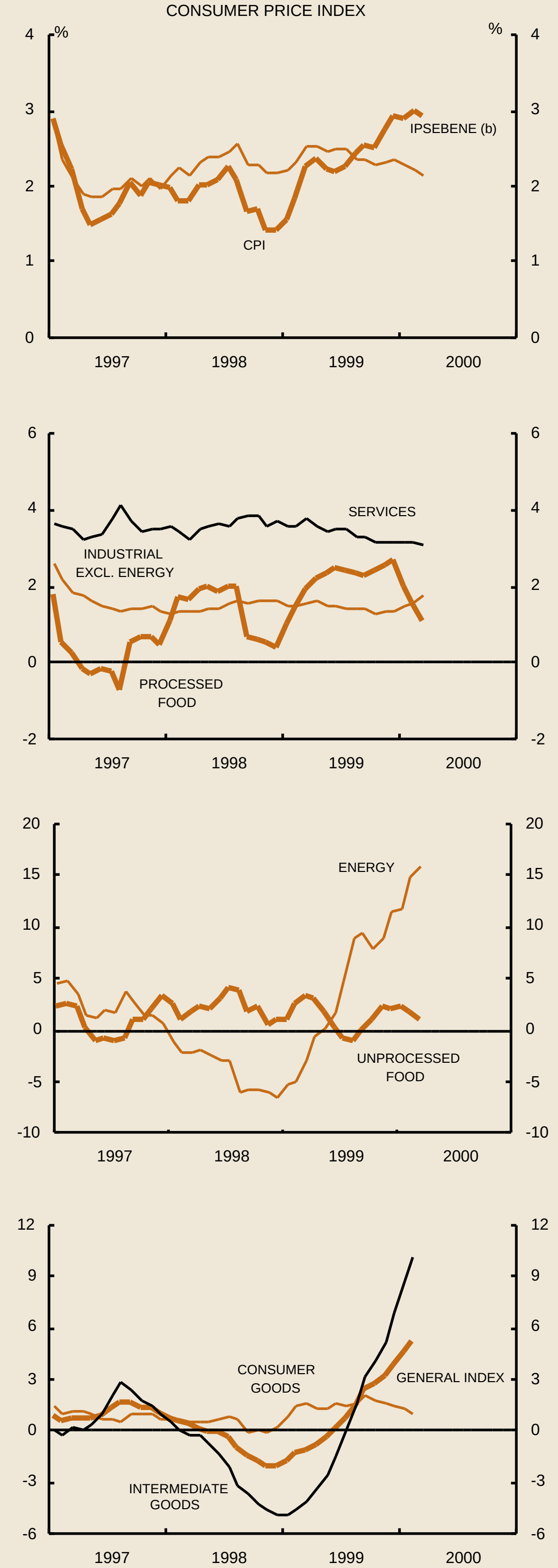


Source: Instituto Nacional de Estadística.
(a) Non-centred annual percentage change, based on QNA trend-cycle series

provided by the EPA for 1999 must be interpreted with caution, as the statistics have been subject to certain modifications within the framework of harmonisation of European labour statistics. These have led to more precise estimation of the level of employment in the Spanish economy, but they have also affected the comparability with past data. This may explain why employment growth at end-1999 was 5.2 % according to the EPA, two percentage points higher than the National Accounts estimate. On EPA data, as regards the length of

CHART 21

Price indicators (a)
Spain



Source: Instituto Nacional de Estadísitica.
(a) Twelve-month percentage change based on the original series.
(b) Index of non-energy processed goods and service prices.

contracts, the year-on-year growth rate of wage-earners with permanent contracts rose in 1999 Q4. However, that of temporary employment recovered to a greater extent, so that the ratio of temporary to permanent employment was slightly up on 1998 Q4, standing at 32.6 %. Both in Q4 and during the year as a whole, part-time employment rose faster than full-time employment, although the results of the new regulations and the establishment of incentives for permanent part-time employment may be considered modest.

According to the EPA, the labour force accelerated in 1999 Q4, rising by 1.8 % year-on-year, twice the rate in Q3. This was due to a significant increase in the participation rate, which stood that 64.1 % for the population between 16 and 64 years of age. The increase in participation cancelled out the rise in employment, leaving the rate of unemployment unchanged from Q3 at 15.4 %. In fact, the rate of decline in the number of persons unemployed fell again, as did that of INEM-registered unemployment in the same period. In 2000 Q1, the rate of decline in registered unemployment was again lower than in the previous quarter, although there were signs of a levelling off. The acceleration in the labour force in 1999 Q4 was greater among women. However, the increase of 8.8 % in female employment meant that female unemployment rates fell, while the male unemployment rate rose slightly.

4.3. Prices and costs

On QNA estimates, in 1999 Q4 the implicit GDP deflator grew by 3.5 % year-on-year, sustaining the upward trend it had displayed throughout the year, to make an average increase of 3.1 % in 1999. As unit labour costs slowed slightly in Q4, and despite the increase in net indirect taxes per unit of output, the acceleration in the deflator was compatible with a significant increase in the gross operating surplus per unit of output and with a widening of margins.

Unit labour costs rose year-on-year by 1.7 % in Q4, one-tenth of a percentage point less than in the previous quarter (see Chart 19), since the recovery in apparent labour productivity made up for the weak acceleration in average remuneration, which increased to 2.4 % from 2.3 % in the previous quarter. According to the Wages Survey, average hourly earnings in 1999 Q4, in terms of total pay, rose by 2.6 % on the same period a year earlier, one-tenth of a percentage point up on the Q3 rate. In terms of average monthly earnings, the increase was slightly smaller (2.5 %), although the acceleration was somewhat greater. Industry by industry, the largest increase in average hourly earnings was in construction (4 %), while in industry (2.6 %) and in services (2.3 %) the increases were considerably more moderate. If these results are compared with those of collective bargaining, an estimate may be obtained for wage drift which, as in recent years, was not significant in 1999. In fact, the average increase in wage rates agreed in 1999 was 2.4 %, without including the effect of inflation-adjustment clauses, which were activated subsequently by the overshooting of the inflation target used as a reference in the settlements.

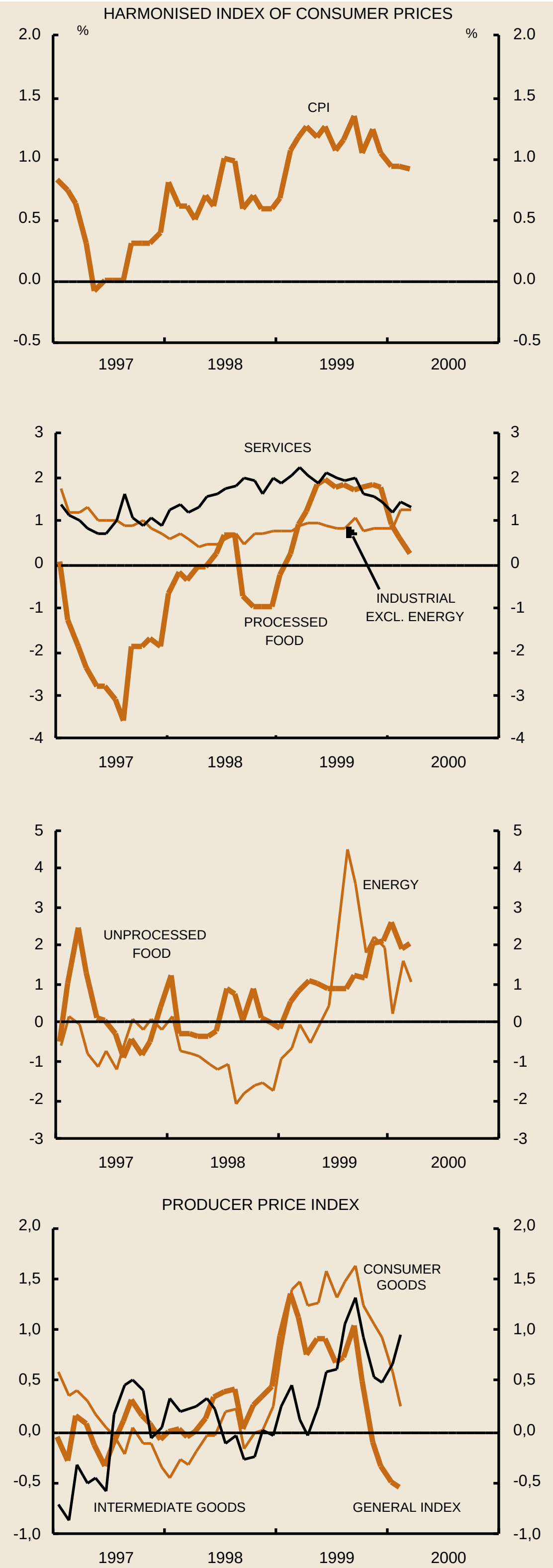
The average increase in wage rates agreed for the year 2000 in the settlements registered to March 31st was 2.8 %, which was higher than in 1999. As usual in the first quarter, most of the registered settlements were under existing agreements. The increase in wage rates under existing agreements to March was 2.7 %. The increase agreed in newly signed agreements was 4.5 %, but this was not a representative figure as very few newly signed agreements had been registered by that date. Industry by industry, the average rise in agriculture was 3.5 %, which was higher than in services (2.8 %), industry (2.7 %) and construction (2.5 %).

Chart 20 shows the behaviour of value-added deflators and unit labour costs in the market economy (excluding non-market services), in industry and in market services. In industry, the value-added deflator accelerated considerably in 1999 Q 4, while unit labour costs moderated, as a consequence of the buoyancy of productivity and the favourable trend in average compensation. As a result, the gross unit operating margin recovered somewhat in the final quarter of 1999. The market services deflator grew at the same rate as in the previous quarter, while unit labour costs rose by two-tenths of a percentage point more than in the Q3. There was thus a narrowing of the gap between these two growth rates, although the unit margin continued to widen.

The upward path of the GDP deflator in 1999 was accompanied by an acceleration in the imports deflator, so that the final demand deflator increased year-on-year by 3.7 % in Q4, eight-tenths of a percentage point more than in Q3. The deflator for goods and services imports rose to a year-on-year rate of 4.6 % in the same period, with an increase in the acceleration that had been taking place over the year. According to the information on import unit value indices, this acceleration continued to increase in January 2000. The growth in import prices was strongly influenced by the prices of

CHART 22

Price indicators
Differential vis-à-vis the euro area (a)



Sources: Eurostat and Banco de España.
(a) Twelve-month percentage change based on the original series.

energy imports, which rose by more than 150 % year-on-year in 1999 Q4, driven by the upward path of oil prices on international markets and, to a lesser extent, by the euro-US dollar exchange rate. The positive growth of non-energy import prices in 1999 Q4 increased in January, in contrast to the declines of the preceding quarters.

Developments in the main price indicators during the first few months of 2000 have continued to be determined largely by the upward path of the price of crude oil on international markets, together with the depreciation of the euro against the US dollar. The 12-month growth rate of the CPI (the main indicator of final prices) stood at 2.9 % in March, close to the end-1999 rate (see Chart 21), despite the decline in the 12-month growth rate of the index of service and non-energy processed goods prices (IPSEBENE) to 2.1 % that month, from 2.4 % in December. The main components of the CPI behaved dissimilarly in the first few months of this year. The strong increase in energy prices and the growth in those of non-energy industrial goods were partly offset by the favourable course of food prices, while service prices held roughly steady.

The 12-month growth rate of the energy component rose from 11.5 % in December to 15.9 % in March. Among energy products, there were significant increases in the prices of both those whose prices are freely determined, such as diesel oil and fuels, and in the case of natural gas, the regulated price of which was increased in February. The decision of OPEC to increase oil production from April will doubtless entail a decline in the oil price on international markets, which will relieve the inflationary pressures stemming from the energy component in the coming months. That said, the reductions in the price per barrel of oil will not be passed through immediately to consumer prices, which will continue to hold at high rates of growth in year-on-year terms. The 12-month growth rate of prices of non-energy industrial goods rose by five-tenths of a percentage point during the first three months of the year, to reach 1.8 % in March. During the same period food prices trended favourably. The 12-month growth rate of the prices of unprocessed food fell by one percentage point to stand at 1 % in March, while that of processed food prices fell from 2.6 % in December to 1.1 % in March. This significant decline is basically a reflection of the fact that the prices of oils increased significantly in the first few months of last year, the period of comparison for the 12-month rate. Finally, service prices rose by 3.1 % in March, with price falls in telecommunications.

The HICP followed a similar path in Spain and in the euro area during the first quarter (see Chart 22). In both cases there was a slight increase in the 12-month rate, which was greater in the case of the euro area. The inflation differential thus narrowed by one-tenth of a percentage point to stand at 0.9 points in March. Component by component, the differential narrowed in the case of food and energy, since the rise in energy prices was stronger in the euro area than in Spain. In the case of services, the differential held steady, while in that of non-energy industrial goods it widened, since the upward path of these prices in Spain was accompanied by a slowdown in the euro area.

The producer price index continued to accelerate during the first two months of the year 2000, to reach a 12-month growth rate of 5.1 % in February, as against 3.8 % in December. The highest growth rates were recorded for energy intermediate goods, although there was also a certain deterioration in the prices of other intermediate goods, as well as capital goods. By contrast, the prices of consumer goods, and food consumer goods in particular, slowed, largely as a result of the high growth rates of olive oil prices in the first few months of 1999, the period of comparison for the 12-month rate. Farm gate prices continued to fall in 1999 Q4, and the information available for the first quarter of the year 2000 on wholesale markets generally indicates that these prices trended favourably.

4.4. State budget

The updated stability programme set a target for the general government deficit for the year 2000 of 0.8 % of GDP, 0.5 percentage points below the deficit then estimated for 1999 (1.3 % of GDP). The year 1999 finally closed with a public deficit of 1.1 % of GDP. The target deficit for general government as a whole in the year 2000 is based on a projected deficit of 0.8 % of GDP for the State and 0.1 % for territorial government, and a surplus of 0.1 % of GDP for the Social Security System.

The first data for the year 2000 in the National Accounts framework, available to March, are consistent with the achievement of this target. In the first three months of the year the State deficit reached approximately PTA 57 billion (0.1 % of GDP), which was very similar to the deficit recorded in the same period of 1999 (see Table 3). Revenue grew by 8 %, basically due to the strength of taxes on consumption, production and imports. As in 1999, the increase in VAT receipts was notable and larger than that explained by its determinants. By con-

TABLE 3

State Budget outturn

PTA bn and %

	Outturn	Percentage change	Budget	Percentage change	Outturn		
	1998	1999/1998	2000		1999 JAN-MAR	2000 JAN-MAR	Percentage change
	1	2	3		5	6	
1. Revenue	**18,364**	**4.8**	**18,742**	**2.1**	**5,001**	**4,866**	**–2.7**
Direct taxes	7,817	4.8	8,008	2.4	1,861	1,738	–6.6
Personal income tax	*5,098*	*2.1*	*5,149*	*1.0*	*1,678*	*1,589*	*–5.3*
Corporate income tax	*2,558*	*10.0*	*2,688*	*5.1*	*130*	*43*	*–66.9*
Other (a)	*161*	*14.9*	*171*	*5.8*	*53*	*106*	*100.9*
Indirect taxes	7,951	13.3	8,558	7.6	2,161	2,505	15.9
VAT	*5,114*	*17.0*	*5,655*	*10.6*	*1,494*	*1,777*	*19.0*
Excise duties	*2,567*	*7.4*	*2,630*	*2.5*	*603*	*657*	*9.0*
Tariffs	*144*	*9.2*	*143*	*–0.9*	*33*	*38*	*12.9*
Other	*126*	*5.3*	*130*	*3.3*	*31*	*34*	*7.6*
Other revenue	2,597	–14.8	2,176	–16.2	979	622	–36.4
2. Expenditure (b)	**19,421**	**4.2**	**19,769**	**1.8**	**5,674**	**5,866**	**3.4**
Wages and salaries	2,979	–2.4	2,888	–3.0	656	628	–4.3
Goods and services	436	12.3	340	–22.0	133	133	0.2
Interest payments	3,178	–4.7	2,806	–11.7	1,593	1,564	–1.8
Current transfers	10,809	9.1	11,664	7.9	2,665	2,930	9.9
Investment	957	2.6	1,012	5.8	409	373	–8.8
Capital transfers	1,063	6.6	1,059	–0.3	218	238	9.2
3. Cash-basis deficit (3 = 1 – 2)	**–1,057**	**–5.1**	**–1,028**	**–2.8**	**–673**	**–1,000**	**48.6**
MEMORANDUM ITEM: NATIONAL ACCOUNTS:							
Revenue	18,796	8.7	—	—	4,573	4,937	8.0
Expenditure	19,882	3.5	—	—	4,623	4,994	8.0
Net borrowing (–) or lending (+) (c)	**–1,087**	**–43.4**	**–788**	**–27.5**	**–51**	**–57**	**12.1**

Sources: Ministerio de Economía y Hacienda and Banco de España.

(a) Including revenue from the tax on the income of non-residents.
(b) Including unclassified expenditure.
(c) The annual figures (columns 1 and 3) are drawn from the Spanish Finance Ministry's response to the Excessive Deficit Procedure questionnaire (ESA 95 methodology).

trast, direct tax receipts grew weakly, and other revenue fell significantly, as a consequence of lower revenue in respect of Banco de España ordinary profits. As for expenditure, it grew by 8 % in March, which was higher than the rate for 1999 as a whole. The decline in final consumption expenditure, associated with the transfer of responsibilities for non-university education to the regional (autonomous) governments, and the related increase in current transfers, as well as the reduction in accrued interest, were notable.

On the available cash-basis information, the State deficit to March 2000 was PTA 1 trillion, as against PTA 673 billion for the same period of 1999. The increase in the cash-basis deficit in 2000 Q1 was due to the reduction in revenue (2.7 %), in contrast to the moderate growth projected in the Budget, and to the 3.4 % increase in expenditure in the first quarter, which was somewhat higher than budgeted. The various items of revenue and expenditure will be discussed below, using cash-basis information.

On the revenue side, total tax receipts grew in line with the budget forecast. However, this aggregate behaviour conceals contrary trends in the various components. While indirect taxes were highly buoyant, direct tax receipts fell significantly in the first quarter. The reduction in personal income tax revenue was largely due to the decline in receipts from the withholdings of regional (autonomous) governments and of social security relating to previous years. Moreover, it should be noted that the withholding tax revenue corresponding to the first two months of 1999 was raised by applying the previous tax regime, with higher withholding rates, and that the rate of withholding tax on dividends has also been reduced in the year 2000. As for corporate income tax, receipts in the first quarter are hardly indicative of their path in the year as a whole, as they were significantly affected by an in-

TABLE 4

Balance of payments: summary table (a)

EUR m

	JAN 1999	JAN 2000
	Receipts	Receipts
Current account	**11,907**	**14,292**
Merchandise	6,894	8,383
Services	3,008	3,431
Tourism	*1,660*	*1,807*
Other services	*1,348*	*1,625*
Income	879	1,116
Current transfers	1,125	1,361
Capital account	**1,559**	**726**
	Payments	Payments
Current account	**13,579**	**16,116**
Merchandise	8,373	10,649
Services	1,988	2,367
Tourism	*316*	*352*
Other services	*1,672*	*2,014*
Income	1,780	1,766
Current transfers	1,438	1,334
Capital account	**61**	**79**
	Balance	Balance
Current account	**–1,671**	**–1,823**
Merchandise	–1,479	–2,265
Services	1,021	1,065
Tourism	*1,344*	*1,454*
Other services	*–324*	*–389*
Income	–900	–650
Current transfers	–313	27
Capital account	**1,498**	**646**

Source: Banco de España.
(a) First provisional results.

crease in rebates and by the change in the tax treatment of non-residents in March 1999 (2).

In the first quarter, the receipts from all the indirect taxes grew at much higher rates than were forecast in the Budget and recorded in 1999 as a whole. As already mentioned, the strength of VAT was notable, with a 19 % rise in receipts in the first quarter. This increase in their growth rate was, to some extent, a consequence of higher energy prices. Among excise duties, the increase in those on tobacco and electricity were notable, as was the tax on certain means of transport, reflecting the significant increase in vehicle registrations.

(2) Revenue from withholdings on interest paid on public debt held by non-residents to February 1999 was included in corporate income tax receipts. Since that date it has been included under the tax on non-residents.

The budget headings covering all other revenue, with the exception of capital transfers (which mostly arise from transactions with the EU), posted lower growth rates than budgeted in the first quarter. The reduction in revenue obtained from the Banco de España, in respect of both capital gains and ordinary profits, was notable, as was the decline in receipts from debt-issuance premiums.

As for expenditure, the growth to March of current expenditure was higher than budgeted, albeit in line with the increase during 1999 as a whole. This overshooting of the Budget projection was basically due to the concentration of interest payments and to the increase in current transfers to territorial government corresponding to their share in State revenue. Within the latter, those to the regional (autonomous) governments grew by almost 40 % to March, as a consequence of the above-mentioned transfers of responsibilities for non-university education in 1999, and of the transfer this year to the Castile and León regional (autonomous) government. By contrast, the contribution to the Social Security System to finance the current transactions of INSALUD (the national health service) rose by 6.4 %, in line with the budget projection, while the contributions to the Community budget declined. As regards capital transactions, investment declined in 2000 Q1, owing to the smaller volume of payments under obligations assumed in previous years, which offset the increase in capital transfers.

Finally, the first data on the budget outturn for the Social Security System in 2000 are briefly discussed. Receipts from social-security contributions (excluding surcharges and penalties) rose by 9.5 % in January, well above the 7.9 % rate projected in the Budget and the 7.2 % increase in 1999 as a whole. The growth in this revenue continued to be driven by the buoyancy of the total number of registered workers, which rose by 5.4 % in 2000 Q1, in line with the increase for 1999 as a whole. On the expenditure side, spending on contributory pensions grew by 4.7 % in January, much more slowly than budgeted. However, this item is expected to accelerate during the year as a result of the increase in minimum pensions and the payment in February 2000 of the compensation for the inflation overshoot in 1999. The number of contributory pensions grew by 1.2 % to March, in line with the budget projection and the increase in 1999. The total number of recipients of unemployment benefits fell by 5 % in February, as against an average reduction of 9.4 % in 1999, reflecting the slower rate of decline of registered unemployment (7 % to February, as against 12.6 % in 1999 as a whole). In line with developments in 1999, the fall in the number of recipients of unemployment benefit was smaller in February than the number of registered unemployed persons hired, so that the eligibility ratio rose (to 65 %, up from 64.5 % in February 1999).

4.5. The Spanish balance of payments and capital account

In January 2000, the current and capital accounts ran an overall deficit of EUR 1,177 million, an increase of EUR 1,003 million on the deficit in the same month of 1999. This outcome reflects the further strong rise (53.2 %) in the trade deficit in the first month of the current year. This was because, although the strong recovery in exports of recent months firmed in January, and imports slowed slightly, there was a further deterioration in the terms of trade, basically due to the notable increase in the prices of imported energy products. The other current-account items, by contrast, trended favourably. The tourism surplus continued to rise and the income deficit narrowed by EUR 251 million, reflecting the improvement in the credit system's income and the reduction in payments made by general government. The balance of current transfers also improved by EUR 340 million, as a consequence of the increase in flows from the EU under EAGGF-Guarantee and the European Social Fund. Finally, the surplus on capital account deteriorated by EUR 851 million in relation to January 1999, due to the lesser buoyancy of structural funds from the EU, although these tend to be subject to delays during the first few months of the year.

The nation's borrowing requirement reflected by these data would indicate a weakening of the sectoral balances of households and firms as a result of the buoyancy of residential investment and the strength of private productive investment, against a background of favourable growth prospects and progress in reducing the budget deficit.

5. Financial flows in the Spanish economy

5.1. Financial flows in the economy as a whole

The information for 1999 Q4 from the financial accounts of the Spanish economy highlights the firming of the trends indicated in previous reports. As can be seen in Table 5, the decline in the nation's net financial saving continued. Taking cumulative data over four quarters, growth stood at –0.9 % of GDP, meaning that the nation's saving was negative for the first time in recent years. This performance was essentially determined by the sharp slowdown in household saving, while the net financial saving of firms diminished only slightly and general government continued to reduce its net borrowing.

In terms of the net financial position, measured as the difference between the stock of financial assets and liabilities, the data for 1999 Q4 confirm the increase in the credit balance of the non-financial corporations and households sector, as has been the case since the early nineties. The increase in the net financial position of firms basically reflects the significant restructuring undertaken in recent years, thanks to more favourable financial conditions and better corporate results. The net financial position of households has been reinforced by the notable rise in the value of their financial wealth and by the change in the composition of their saving in favour of financial instruments offering greater capital-gains generating capacity, rather than by an increase in assets purchased.

Turning to the financial account of the balance of payments, net capital outflows were recorded in 1999, as in the previous year. In other words, the Spanish economy invested more financial resources abroad than those it obtained from non-residents, whereby net assets vis-à-vis the external sector (excluding reserves) increased by EUR 12 billion (see Table 6). The significant rise in net capital outflows is mainly due to the strong buoyancy of Spanish direct and portfolio investment abroad, which amounted to EUR 76 billion, equivalent to 14 % of GDP. The salient event during the year was undoubtedly the exceptional expansion of direct investment abroad which, at EUR 33 billion, was double the previous year's figure.

As regards other investment, 1999 saw a change in the composition of foreign assets, with a notable reduction in non-financial private-sector deposits in non-resident banks. That suggests that agents, given unified payment systems in the euro area, have opted to cancel a portion of their previous positions. In turn, the foreign assets of the credit system increased forcefully, this being mainly the outcome of the increase in the intra-system assets held by the

TABLE 5

Saving and financial position

	FINANCIAL SAVING AS % OF GDP (Cumulative data over four quarters)										
	Average 1988-1992	Average 1993-1997	1997	1998				1999			
				Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Financial saving of the nation	–2.7	0.5	1.5	1.3	1.0	1.1	0.9	0.9	0.7	0.2	–0.9
Non-financial corporations and households	–0.2	4.9	3.1	2.6	2.0	2.1	1.7	1.6	1.2	0.9	–0.3
Non-financial corporations	*–4.0*	*–0.7*	*–0.8*	*–0.3*	*–1.0*	*–0.9*	*–1.0*	*–0.8*	*–0.6*	*–1.0*	*–1.2*
Households	*3.8*	*5.6*	*3.9*	*2.9*	*3.0*	*2.9*	*2.7*	*2.4*	*1.8*	*1.9*	*0.9*
Credit institutions (a)	1.4	0.7	0.6	0.7	0.8	0.6	0.6	0.5	0.4	0.4	0.4
Institutional investors (b)	–0.2	0.1	0.2	0.2	0.1	0.1	0.1	0.1	0.1	0.1	0.1
General government	–3.8	–5.4	–2.4	–2.2	–2.0	–1.7	–1.7	–1.4	–1.1	–1.2	–1.1

	FINANCIAL POSITION AS % OF GDP (c) (Fourth-quarter data)							
	1992	1993	1994	1995	1996	1997	1998	1999
Financial position of the nation	–16.7	–19.2	–19.4	–18.0	–17.7	–18.1	–19.2	–20.4
Non-financial corporations and households	39.8	48.1	53.2	59.2	68.5	77.2	86.2	95.9
Non-financial corporations (d)	*–17.3*	*–16.4*	*–13.6*	*–10.9*	*–6.7*	*–4.8*	*–0.3*	*5.4*
Households	*57.1*	*64.5*	*66.8*	*70.1*	*75.2*	*82.0*	*86.5*	*90.6*
Credit institutions (a) (d)	12.5	14.1	13.0	12.1	12.8	14.2	14.2	14.2
Institutional investors (b)	–1.1	–1.2	–1.0	–0.9	–0.6	–0.5	–0.6	–0.6
General government	–35.2	–42.3	–46.5	–50.3	–52.6	–52.0	–49.7	–47.5

Source: Banco de España.

(a) Defined according to the 1st Banking Directive.
(b) Insurance companies, portfolio investment institutions and securities-dealer companies and securities agencies.
(c) Calculated as the difference between outstanding financial assets and liabilities.
(d) Liabilities do not include shares.

Banco de España, and whose origin is linked to the interbank operations transacted via the TARGET system. The decline witnessed in reserve assets is in response to the transfer of reserves from the Banco de España to the ECB at the beginning of the year and to the maturity of foreign exchange swaps previously entered into.

Concerning purchases of external liabilities (capital inflows), the most notable development is the appreciable increase in non-resident portfolio investment, which amounted to EUR 41 billion. Unlike the previous year, in which over half the total of portfolio investment took the form of equity purchases, the slackness of national stock markets for much of 1999 shifted investors' attention towards government debt securities. With respect to other foreign liabilities included under the heading of other investment, there were two notable aspects. On one hand, the high foreign indebtedness of the non-financial private sector (which, in part, has been instrumental in financing Spanish firms' direct investment transactions abroad). And on the other, the increase once again in credit institutions' foreign liabilities, although the rate of their indebtedness was less than in 1998.

With regard to the sectoral structure of financial flows, the net capital outflows recorded during 1999 were mostly determined by the net acquisition of foreign assets by the non-financial private sector. This was financed via the indebtedness of the credit system (excluding the Banco de España) and the acquisition of government debt by non-resident investors.

Into the year 2000, there is only balance of payments information for January, which may not prove very relevant as regards the potential patterns to be expected this year. In any event, the main development for this month is that there was a net capital inflow, part of which was due to a direct investment flow from abroad into Spain. The flow was relatively high and exceeded that of Spanish direct investment in other countries.

5.2. Financial flows of households and non-financial corporations

As discussed in the previous section, the net financial saving of the non-financial private sector fell notably in 1999 Q4 to -0.3 % of GDP (on

TABLE 6

Balance of payments on financial account

EUR m

	1997	JAN-DEC 1998	JAN-DEC 1999
BALANCE ON FINANCIAL ACCOUNT	**–2.775**	**–991**	**9.098**
CHANGE IN LIABILITIES VIS-À-VIS EXTERNAL SECTOR	**34.479**	**65.678**	**88.157**
Direct investment (a)	**5.621**	**10.151**	**8.819**
Portfolio investment (b)	**11.068**	**15.353**	**41.419**
General government	9.952	4.125	23.812
Other resident sectors	1.183	8.469	9.348
Credit system	–67	2.759	8.259
Other investment	**17.790**	**40.174**	**37.919**
General government	21	866	–356
Other resident sectors	544	4.318	13.846
Credit system	17.226	34.990	24.429
CHANGE IN ASSETS VIS-À-VIS EXTERNAL SECTOR	**37.255**	**66.669**	**79.059**
Direct investment	**10.970**	**16.507**	**32.658**
Other resident sectors	9.844	14.756	33.199
Credit system	1.126	1.751	–541
Portfolio investment	**14.377**	**40.787**	**43.170**
Other resident sectors	10.049	29.873	29.302
Credit system	4.328	10.914	13.868
Other investment	**1.555**	**21.623**	**24.202**
General government	331	388	213
Other resident sectors	12.392	17.668	–8.853
Credit system	–11.168	3.567	32.842
Reserves	**10.352**	**–12.248**	**–20.971**

Source: Balance of Payments. Banco de España.
(a) Includes portfolio investment in unlisted shares.
(b) Includes direct investment in listed shares.

cumulative data over four quarters). This was particularly due to the heavy fall in household saving, the result of the growth of liabilities outpacing that of financial assets. According to the estimates based on the provisional information available for certain financial asset and liability items, this trend might hold in 2000 Q1.

Turning to financial assets, Table 7 and Chart 23 show how, from January to March 2000, private-sector financial investment may have sustained a stable growth rate of around 14 % compared with a year earlier, virtually unchanged on the second half of 1999. Conversely, it is estimated that liquid financial assets (comprising cash, bank deposits, repos, bank securities and shares in fixed-income mutual funds) have continued to grow at a much more moderate rate than total financial assets, running at a stable year-on-year rate of around 3%. The rate of expansion of cash and cash equivalents moderated appreciably in 1999 Q4. As a result, its annual growth rate stood at 12 % at end-1999, compared with 17 % in previous quarters. Foreseeably, it will have continued on this trend in the January-March period in 2000. The relative restraint of cash and cash equivalents (which is most likely associated with the higher opportunity cost of holding such assets given rising interest rates) might be interpreted as a sign of agents' lesser willingness to adopt immediate spending decisions. However, the related rates of expansion remain very high and, moreover, the biggest slowdown appears to be for firms whereas it is less significant for households, where the relationship between cash and cash equivalents and spending decisions may be more direct.

As regards private-sector financial liabilities, the expansionary trend of previous quarters, with growth running at around 16 %, has been sustained. This figure reflects the firming of high rates of increase in finance extended to the private sector. Indeed, the indebtedness aggregate made up of bank credit and fixed-income securities is estimated to have grown at a rate of 20% in 2000 Q1 compared with a year earli-

TABLE 7

Financial assets and liabilities of households and non-financial firms

	Latest quarter balance (a) (b)	Four-quarter % change					
		1998	1999				2000 (b)
		Q4	Q1	Q2	Q3	Q4	Q1
HOUSEHOLDS AND NON-FINANCIAL CORPORATIONS:							
Total financial assets	**1.423.6**	**14.3**	**10.9**	**12.0**	**14.2**	**14.2**	**14.6**
Liquid financial assets	549.5	5.4	4.3	4.2	4.3	2.8	2.5
Cash and cash equivalents	*271.8*	*14.6*	*14.9*	*17.5*	*17.5*	*11.9*	*12.5*
Other liquid financial assets	*277.6*	*–1.1*	*–3.1*	*–5.5*	*–5.4*	*–4.7*	*–5.7*
Other financial assets	874.2	22.6	16.6	18.5	22.4	23.3	23.8
Total liabilities	**938.0**	**13.2**	**14.4**	**16.3**	**16.4**	**15.8**	**16.2**
Bank financing plus fixed-income securities	618.4	16.2	15.9	19.2	19.3	19.0	20.0
Credit from resident credit institutions	*481.8*	*15.7*	*14.8*	*16.6*	*15.9*	*15.6*	*16.5*
Other financial liabilities	319.6	8.3	12.0	11.4	11.4	10.2	9.4
HOUSEHOLDS:							
Total financial assets	**905.2**	**12.8**	**8.5**	**8.9**	**11.3**	**11.6**	**12.0**
Liquid financial assets	446.8	3.6	2.2	1.6	1.1	0.7	0.3
Cash and cash equivalents	*204.9*	*8.9*	*10.6*	*14.2*	*15.4*	*13.9*	*12.7*
Other liquid financial assets	*241.9*	*0.4*	*–2.8*	*–6.3*	*–7.9*	*–8.2*	*–8.3*
Other financial assets	458.4	27.4	17.2	18.8	26.2	25.8	26.3
Total liabilities	**380.0**	**13.2**	**15.4**	**15.1**	**15.3**	**14.6**	**12.7**
Bank financing plus fixed-income securities	272.7	18.3	18.5	18.3	18.3	17.7	16.0
Credit from resident credit institutions	*246.9*	*19.1*	*19.3*	*19.0*	*18.9*	*18.2*	*16.3*
Other financial liabilities	107.3	3.0	8.8	8.2	8.8	7.4	5.2
NON-FINANCIAL CORPORATIONS:							
Total financial assets	**518.4**	**17.3**	**15.8**	**18.0**	**19.4**	**19.0**	**19.5**
Liquid financial assets	102.7	14.8	15.5	17.7	21.3	13.0	13.5
Cash and cash equivalents	*67.0*	*35.4*	*30.2*	*28.8*	*24.6*	*6.1*	*11.7*
Other liquid financial assets	*35.7*	*–13.5*	*–5.4*	*1.4*	*16.2*	*27.8*	*16.8*
Other financial assets	415.7	18.0	15.9	18.1	18.9	20.7	21.1
Or which: *Claims on non-financial corporations and households*	*192.6*	*8.3*	*8.5*	*9.0*	*8.1*	*8.9*	*13.9*
Claims on rest of the world	*126.7*	*48.4*	*37.3*	*41.7*	*39.9*	*38.1*	*38.3*
Total liabilities	**558.0**	**13.2**	**13.8**	**17.2**	**17.2**	**16.7**	**18.6**
Bank financing plus fixed-income securities	345.7	14.5	13.7	19.9	20.2	20.0	23.3
Credit from resident credit institutions	*235.0*	*12.5*	*10.4*	*14.2*	*13.0*	*13.0*	*16.7*
Other financial liabilities	212.3	11.3	13.9	13.1	12.8	11.7	11.7

Source: Banco de España.
(a) EUR billions.
(b) The data for 2000 Q1 are provisional estimates.

er, one percentage point up on the end-1999 rate.

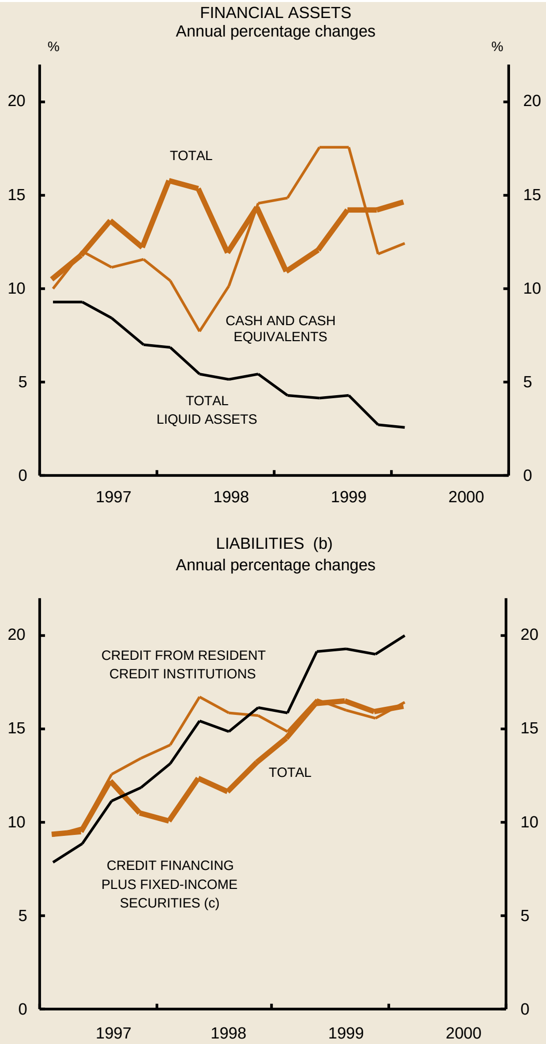
5.2.1. Financial flows of households

The most significant development in respect of household finances during 1999 Q4 was the fact that their net financial saving diminished drastically to 0.9 % of GDP, the lowest level of the past two decades. This has come about due to a series of factors that have encouraged spending and debt to the detriment of saving. Such factors include most notably: the increase in the financial wealth of the sector, underpinned above all by the rise in stock market prices; favourable finance conditions, which have been conducive to households incurring bank debt at a notable rate; and, lastly, the favourable economic outlook, which leads to a reduction in precautionary saving.

In 2000 Q1, in line with recent quarters, the growth of assets has accelerated slightly while the pace of liabilities has moderated (see Chart 24). It is estimated that total financial assets have grown in this period at a year-on-year rate of 12 % (similar to end-1999). In terms of their

CHART 23

Non-financial corporations and households (a)



Source: Banco de España.
(a) The data for 2000 Q1 are provisional estimates.
(b) Excluding shares.
(c) Excluding trade credit.

composition, the contribution of liquid financial assets has once more remained very moderate, running at a rate of virtually zero (0.3 %). Both cash and cash equivalents and the remaining liquid assets appear to have held at a stable growth rate compared with 1999. Thus, the former posted a rate of increase close to 13 % year-on-year, while the growth rate of other liquid assets was negative of the order of 8 %. In this respect, the most salient development in recent months has been the shift in saving from fixed-income mutual funds towards other financial instruments, such as deposits with an agreed maturity, equity and international funds, and insurance products. Among the latter, demand appears to be concentrated in unit-linked funds, which offer an attractive, tax-efficient return.

The expansion of household financial liabilities, which had exhibited a very high growth rate throughout 1999 (15 %), may have moderated in 2000 Q1 to a rate below 13 % year-on-year. The rate of advance of finance obtained via resident credit institutions, the main source of finance for this sector, has fallen to 16 % year-on-year, two percentage points down on the end-1999 rate. Drawing on information on the end-use of credit in 1999 Q4, credit extended for house purchases is holding at a high rate of 19 %, while that to finance durable goods acquisitions has, in line with the trend throughout the year, moderated appreciably to 8 % in relation to the same period a year earlier.

5.2.2. Financial flows of non-financial corporations

The financial flows of firms show the respective growth rates of financial assets and liabilities to be more balanced than in the case of households. That has made for stable net financial saving in this sector, which stood at –1.2 % of GDP in 1999 Q4. This level, similar to that seen in recent years, shows that firms are financing the current phase of economic growth without having to incur significant debt in net terms. The sector is therefore generating a high volume of own resources to finance its investments and, moreover, Spanish firms are clearly targeting more of their investment abroad. In fact, irrespective of whether financing is via debt or capital increases, the external expansion of corporate activity does not affect net financial saving, since it involves in parallel an increase in the financial assets held by firms.

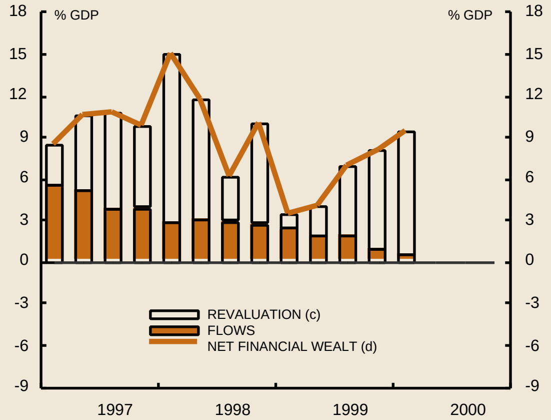
With regard to recent developments in financial assets, these were as buoyant in 2000 Q1 as in previous periods. The growth of total financial assets could be close to 20 % compared with the same period in 1999. As in previous periods, it is the less liquid financial instruments which continue to make the highest contributions (see Chart 25), and notable among these are assets vis-à-vis households and firms (so-called inter-company credit), and claims on the rest of the world.

In parallel with the growth of financial assets, it is estimated that firms' financial liabilities increased considerably in 2000 Q1, up to a rate close to 19 % year-on-year, two percentage points higher than the end-1999 rate. This rise is attributable to the increase in credit obtained both from the resident banking system and from other households and firms, the year-on-year growth rates for both of which increased by

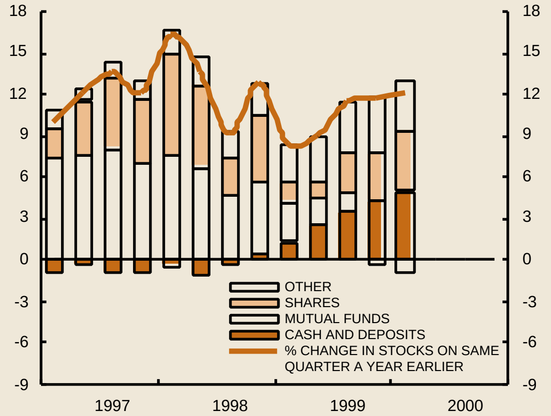
CHART 24

Households (a)

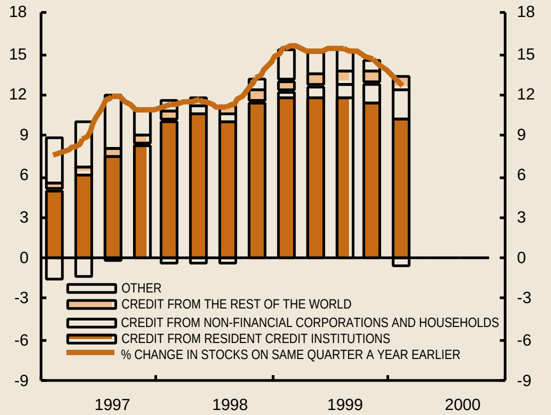
ANNUAL PERCENTAGE CHANGE IN NET FINANCIAL WEALTH AND CONTRIBUTIONS (b)



CONTRIBUTION OF THE VARIOUS INSTRUMENTS TO THE GROWTH OF FINANCIAL ASSETS



CONTRIBUTION OF THE VARIOUS INSTRUMENTS TO THE GROWTH OF LIABILITIES



Source: Banco de España.

(a) The data for 2000 Q1 are provisional estimates.

(b) The flows and revaluation are cumulative data over the latest four quarters.

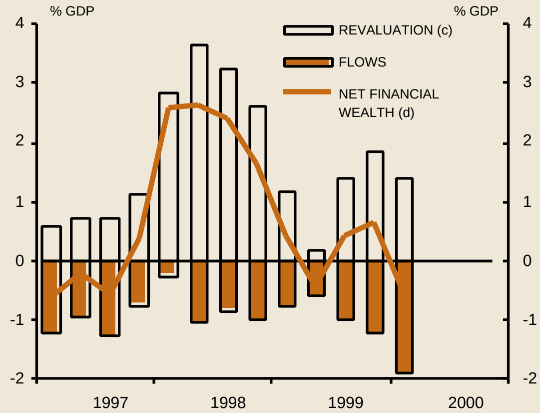
(c) Difference between the change in the stock and the flow.

(d) Calculated using an estimate of the assets valued at market prices.

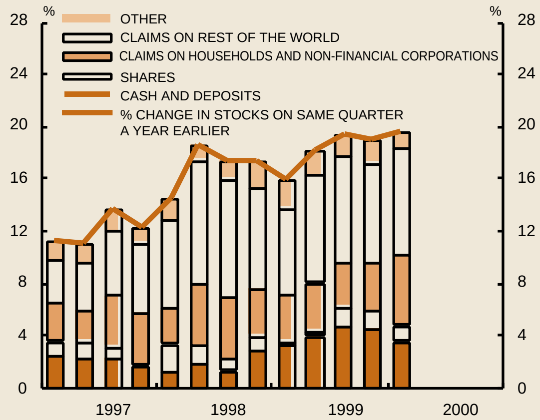
CHART 25

Non-financial corporations (a)

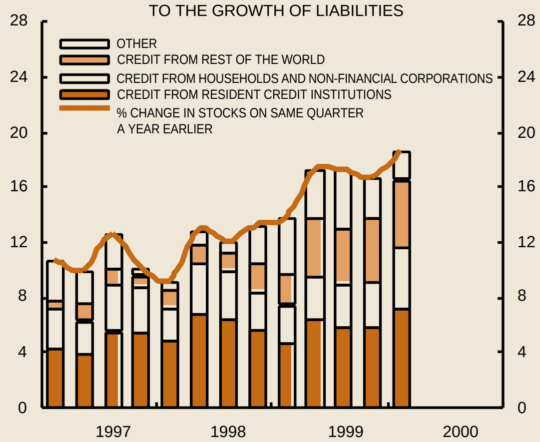
ANNUAL PERCENTAGE CHANGE IN NET FINANCIAL WEALTH AND CONTRIBUTIONS (b)



CONTRIBUTION OF THE VARIOUS INSTRUMENTS TO THE GROWTH OF FINANCIAL ASSETS



CONTRIBUTION OF THE VARIOUS INSTRUMENTS TO THE GROWTH OF LIABILITIES



Source: Banco de España.

(a) The data for 2000 Q1 are provisional estimates.

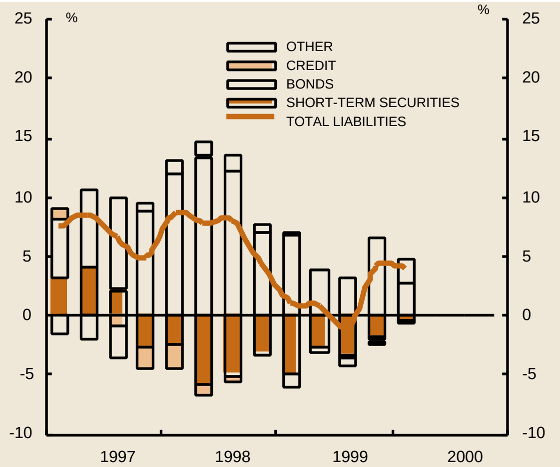
(b) The flows and revaluation are cumulative data over the latest four quarters.

(c) Difference between the change in the stock and the flow.

(d) The liabilities do not include shares. Calculated using an estimate of the assets valued at market prices.

CHART 26

Growth of general government liabilities



Source: Banco de España.

around four points in relation to the previous quarter.

Information on the destination of bank finance for 1999 Q4 shows notable restraint in lending extended to productive activities. The related growth rate was 12 %, four points down on the previous quarter. This restraint was due to the reduction in credit extended to the industrial sector and to services, which ended the year expanding at respective rates of 9 % and 11 %, six percentage points down on the previous quarter in both cases. Nonetheless, credit to construction activity held on a rising trend, running at 20 % year-on-year, five points above the rate for the preceding quarter.

5.3. General government financial flows

Cumulative general government net borrowing during the four quarters to 1999 Q4 fell to 1.1 % of GDP, three-tenths of a point below the budget target set at the beginning of the year. The information available for 2000 Q1 suggests this improvement has continued, with the estimated net financial saving for the sector as a whole in line with that budgeted for the entire year.

Unlike in previous quarters, financial liabilities have recently been on a rising course (see Chart 26), running at a year-on-year rate of change of 3 % in 1999 Q4, a very similar rate to that expected for 2000 Q1. This does not contradict the data on the course of net financial saving, since this also depends on changes in financial assets. Moreover, the pattern of interest payments in the opening months of the year has meant that net borrowing in this period has been greater than in previous years, without this bearing on the annual targets set.

Notable in connection with the composition of the stock of financial liabilities was that throughout 1999 there were positive net issues of long-term liabilities, while the stock of short-term instruments diminished drastically. This meant that, at end-1999, the average life of peseta-denominated government debt was 5.3 years, compared with five years at the close of 1998. In the period from January to April 2000, there have been negative net issues of public securities for an amount of EUR 1.7 billion, the result of redemptions of both long- and short-term borrowings for EUR 0.6 and 1.1 billion, respectively. Nonetheless, in the case of medium- and long-term debt, this figure is strongly influenced by the sizeable redemption of three-year bonds that took place in mid-April. Accordingly, these funds may once more be re-invested in medium- and long-term bonds at the related May tenders. The outstanding balance of six- and twelve-month Treasury bills has declined, while that of 18-month bills has increased.

26.4.2000.